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Regulation

March/Apr 1979 AEI Journal on Government and Society

NEEDS AND LICENSES
Michael Pertschuk

SACCHARIN AND HUMAN RISK
William R. Havender

THE PRESIDENT'S COMMISSION ON ANTITRUST
Joe Sims

RACIAL REASONING IN UNFREE MARKETS
Walter Williams

NEIL STAEBLER REFLECTS ON THE ELECTION COMMISSION

Smoking and the Advertising Ban
Gideon Doron

The Sears Catalog of Litigation
Bubbles at EPA • No Confidence in Old Trusts
Sour Lemons at the FTC

READINGS OF PARTICULAR INTEREST

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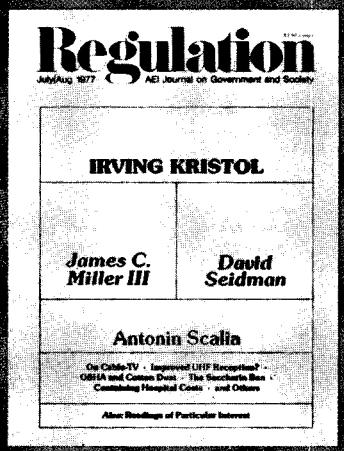
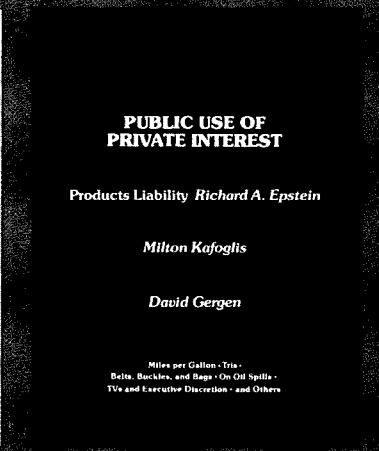
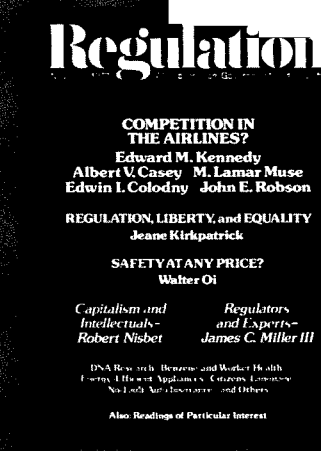
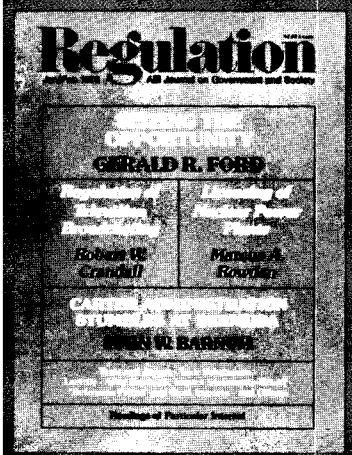
Q. WHAT'S BECOME THE NUMBER ONE REGULATION IN THE U.S.A.?

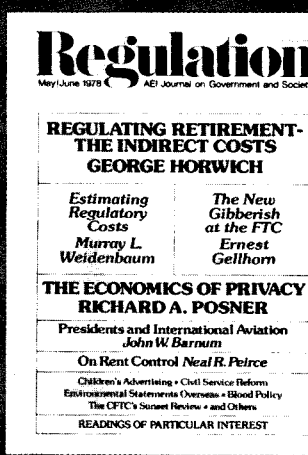
A.

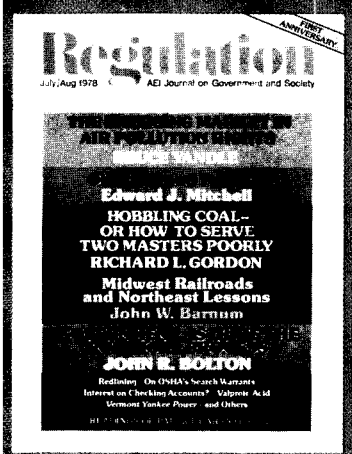


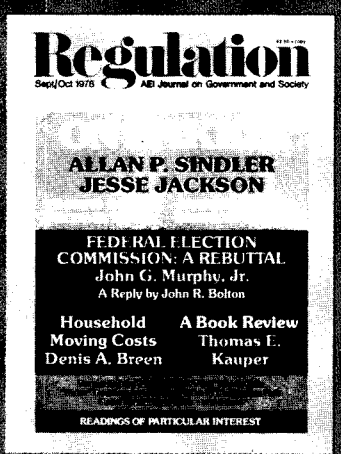


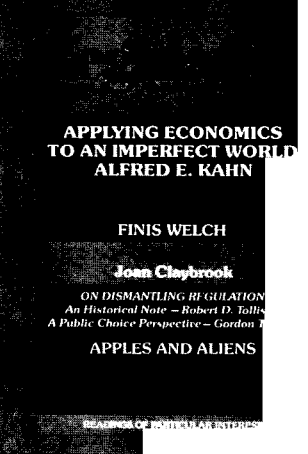











APPLYING ECONOMICS TO AN IMPERFECT WORLD
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Regulation

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Letters

We welcome letters from readers, particularly commentaries that reflect upon or take issue with material we have published. The writer's name, affiliation, address, and telephone number should be included. Letters are subject to abridgment.

The Minimum Wage

TO THE EDITOR:

Allow me to add one more facet to Finis Welch's perceptive discussion of "The Rising Impact of Minimum Wages" (*Regulation*, November/December 1978). A U.S. minimum wage in excess of 40 percent of the average manufacturing wage is almost certainly a major contributor to the heavy flow of illegal alien workers into the United States, since, as World Bank data strongly suggest, the average wage in Mexico is no more than 35 percent of the average U.S. manufacturing wage. Thus, the U.S. minimum wage makes it illegal to hire *any* workers in the United States unless they are paid wages above those the *majority* of Mexican workers can earn in their own nation. One must expect the more able and adventurous of them to seek their fortunes where no local competition is permitted—offering to work for, say, 30 percent more than they can make at home. Entering illegally, they generally will not wish to risk discovery by accepting valuable but costly fringe benefits, and they will be willing and hard workers.

The 35 percent figure is calculated from data presented in *World Development Report, 1978* (World Bank, August 1978). GNP per capita is adjusted by the percentage of population of working age (51 percent in Mexico, 64 percent in the United States) to approximate the annual income per worker. This yields per worker income of $2,137 for Mexico and $12,328 for the United States (only an approximation because the GNP data are for 1976 and the labor force data for 1975). On this basis, average Mexican wages are only 17.3 percent of average U.S. wages. But this is surely an underestimate. If we adjust by using "international" dollars to improve the comparison (according to World Bank figures), we come up with an adjustment factor something less than two. (No Mexican data are given by the World Bank, but the "less than two" figure is suggested by the data for other nations.) Doubling the 17.3 percentage gives us the 35 percent estimate taken here to approximate the upper bound.

The artificially maintained high wage, like any artificially engineered price, invites entry and expansion. If it is a legal barrier, it results in illegal activity. In this case it complicates international and diplomatic relations as well.

Dean A. Worcester, Jr.,
University of Washington

TO THE EDITOR:

Just a small clarification of a passing reference to my work in Finis Welch's excellent report on "The Rising Impact of Minimum Wages."

The quote is: "As Jacob Mincer showed in his article in 1976, no firm theoretical predictions can be made for the effects of minimum wages on measured *unemployment*." The small correction that is needed is to italicize the word measured rather than the word unemployment. I suggest this for two reasons—because unemployment is measured with greater error than employment, and because labor turnover and therefore "frictional" unemployment may decrease in consequence of minimum wage hikes. Neither Welch nor I consider this to be very likely, but the possibility cannot be rejected.

We may define "frictional" unemployment as what occurs when the number of unemployed job seekers is equal to the number of vacancies, while "permanent" unemployment is the case when the number of unemployed job seekers exceeds the number of vacancies. My analysis showed unambiguously that the imposition of (or increase in) minimum wages creates (or increases) "permanent" unemployment, whether or not "frictional" unemployment also changes. Of course, no qualifications attach to the unambiguously predicted reduction of low-wage workers.

Jacob Mincer,
Columbia University

FINIS WELCH responds:

As usual, Jacob Mincer is absolutely right.

Dean A. Worcester is more convinced than I am that U.S. minimum wage legislation contributes to the inflow of undocumented alien workers. The effect could in fact go either way.

For firms covered by and complying with the legislation, the effect is almost certainly to reduce work opportunities for the undocumented. As is true for any other group, if in the absence of the legislation a disproportionate number of undocumented workers would earn low wages, then a minimum wage discriminates against their being employed.

For firms not covered by the legislation, a minimum that restricts employment in covered sectors increases the number of low-wage workers seeking jobs in uncovered sectors and operates to the disadvantage of any (low-wage) group seeking jobs in those sectors.

This leaves us with firms in the covered sector that are willing to risk noncompliance. Much of the onus for detecting noncomplying employers falls on employees. The incentive to report one's employer for paying less than the minimum lies in the possibility of recouping the full difference between the minimum and the wage actually paid. But if an undocumented worker increases his own chance of deportation by reporting his employer, the incentive to report is clearly reduced. Thus it is probably true that a noncomplying firm stands a reduced chance of detection by employing the undocumented.

It is uncertain whether the implicit incentive for noncompliance through the employment of undocumented workers would have effects stronger than the direct effects of compliance in the complying firms. But even if Professor Worcester is right—even if minimum wages on balance contribute to the inflow of "illegals"—I am not convinced that this result is an additional disadvantage of the law. It may, in fact, be one of the few advantages.

But that is a subject for another day.

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What Price Safety?

TO THE EDITOR:

Joan Claybrook ("Crying Wolf," *Regulation,* November/December 1978) seems to believe that the auto manufacturer will not give the people what they want unless she compels it to do so. This belief shows a profound ignorance of the workings of the market economy. Actually, of course, the market system itself is a disciplining instrument. Auto makers are confronted by consumers with different degrees of aversion to risk, different income constraints, and different rates of discount applied to future benefits. The market compels the auto makers, if they are to be successful, to offer models with differing properties (degrees of safety, and so on): the people then freely choose among the alternatives offered, given their aversion to risk, their income, and their individual discount rate.

When Miss Claybrook requires some higher safety standard than would otherwise be produced, she is doing auto buyers a disservice. She requires them to purchase more safety than they want, at the expense of other commodities they would prefer. A student of economics would say that she has pushed consumers to a lower indifference surface and therefore has made them worse off. Consumer advocate, indeed!

Nor can much be said for her sense of ethics. She would undoubtedly rail against deceptive advertising by others, but she engages in the practice herself. She tells us that the "average cost to consumers of safety features contained in a model year 1978 automobile [is] about $250" and that the General Accounting Office "estimated in 1974 that vehicle safety standards had saved some 28,000 lives over the years from 1966 to 1974." Some comparison!

The *cost* is decomposed to a per car estimate. It is given as $250 per car, not as $250 per car times some 12,000,000 cars produced each year times eight years—for a total of $24 billion. The number of lives saved, in contrast, is given as an eight-year total of 28,000 lives, not as an annual average of 3,500 lives. Moreover, with total cars in use of 120 million (based on an average of about ten years of use per car), this turns out to be one death avoided for 3,430 cars in which the investment in improved safety has been made. If one sees the side-by-side appearance of $250 and 28,000 lives, one might be forgiven for believing that the safety standards imposed by Miss Claybrook and her colleagues are "one of the car buyer's best investments." However, if one compares $24 billion and 28,000 lives (or costs of $250 per car for 3,430 cars for every life saved), it becomes far less clear that this represents the best use for a car buyer's money or for the social resources of the community.

Miss Claybrook says that the regulations promulgated but not yet effective—for upgraded bumpers, passive restraints, and greater fuel economy—will add $300 (1977 figures) to the price of a passenger car by 1984 but will save the consumer $890 (post-1977 depreciated figures) over the life of the car. This exchange, she says, "does not appear to be disadvantageous to the consumer." Whether it is disadvantageous depends, of course, on the rate at which the consumer discounts future benefits. That rate will vary among consumers. Some will think it wise to invest $300 at the time of vehicle purchase in order to receive $890 over the life of the vehicle; others will not.

If Joan Claybrook's discount rate is such that she would make that investment, she should be given the opportunity to do so. But others with other discount rates ought not be required to make the investment. In any case, if she truly believes consumers are helped by the investment, she ought to be prepared to let them make the choice freely. She does not. She *compels* them to invest in safety equipment—which suggests that she knows they will not do it without compulsion, which suggests they may be better off not doing it.

Finally, she violates some primitive principles of statistical inference when she says "the procession of recalled vehicles" indicates "a certain laxity of quality control." This may indicate only that Joan Claybrook and her like have a passion for imposing their standards on others. If she really wants to do consumers a service, she might think about getting off their backs.

Simon Rottenberg,
University of Massachusetts

TO THE EDITOR:

Ms. Claybrook in "Crying Wolf" is correct to fault those in business who seek government subsidies while deriding government regulation. After all, if government becomes part-owner of a business enterprise, it is not surprising that it would wish to be part-controller as well.

She is, however, incorrect in making it appear that the demand for deregulation is merely an expression of the wishes of corporate America—a designation that is, in any case, annoyingly vague. There are serious observers without any vested corporate interest who regard deregulation as a fine thing....

Admittedly, Ms. Claybrook has a point about those who advocate deregulation primarily on grounds that it will lower costs. But not everyone advances this argument—making it appear that cost and benefit are all. There are those who regard the *methods* of government regulation as quite intolerable. Ms. Claybrook claims that government regulation promotes "the general welfare" and is therefore, at least as she practices it, a legitimate government function. But the general welfare is supposed to be pursued within the framework of principles established in the Bill of Rights. However that is not how government proceeds when it regulates business. Such regulation is commonly preemptory. It is tantamount to punishing individuals not for what they have done but for what they *might* do or have the opportunity of doing. The entire government regulatory establishment, in fact, violates the spirit of the Bill of Rights—the spirit that insists upon the presumption of innocence until it is demonstrated that a *crime* has been committed and by the person who is to bear the punishment. . . .

The central indictment of government regulation, from my point of view, lies not in costs and benefits but in the fact that it violates human rights on various fronts. That its costs exceed its benefits merely shows that injustice breeds imprudence.

Tibor Machan,
SUNY College, Fredonia

JOAN CLAYBROOK responds:

I would like to comment on several points in the letters from Tibor Machan and Simon Rottenberg. Machan apparently thinks the Bill of Rights . . . is designed to protect business from so-called "preemptory" regulation. Perhaps he is thinking about the Administrative Procedure Act under which regulatory decisions must be based on

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the public record, must meet statutory criteria, and must not be arbitrary and capricious. While that act is important, it is not a bill of rights for regulated business. It is designed to protect the interests of all parties concerned with regulatory action, including consumers and the public in general.

Machan also suggests that regulation is tantamount to punishing individuals not for what they have done, but for what they might do. Safety regulation is normally imposed following gross abuses that the marketplace does not correct. Its purpose is to prevent the recurrence of certain harm, not to punish. Machan expresses great concern for human rights. What about the rights of individuals to breathe clean air, to drink clean water, to secure drugs and food that do not have unnecessary side effects or cause illness, to have a job that does not foster cancer, to drive an automobile without unnecessary exposure to death or crippling injury? These are rights of the citizenry which regulation is designed to defend.

Mr. Rottenberg suggests I am mistaken in advocating regulation for safer cars, since the marketplace can do the job. As any economist knows, two necessary conditions for the marketplace to function effectively are the inability of any seller to control markets and substantial knowledge on the part of consumers. Neither of these conditions is met in the U.S. automobile market. The auto manufacturing industry is oligopolistic and consumer knowledge is far from complete. There are less than fifteen firms of any significance selling cars in the United States today, and the two largest account for more than 70 percent of the production. In addition, how many auto companies advertise the relative safety of their vehicles or inform users of the risk of being in an accident. How many advertised the fuel efficiency of their vehicles six years ago? The marketplace has long been recognized as inadequate to protect legitimate health and safety rights against incursions such as pollution and latent defects.

Mr. Rottenberg takes great pleasure in refuting some of the numbers in my article, but he makes several dispositive errors. He fails to recognize that, even without additional regulations, the existing requirements will reap benefits over the ten-year cycle of the vehicle fleet. Thus, each succeeding year brings more benefits relative to cost. Also, his arithmetic is wrong. He assumes that the cost for the safety standards was $250 per car since 1966. It was zero in 1966 before any standards were issued and the numbers for each year thereafter were rather small. It reached $250 only in 1978. Rottenberg assumed it was $250 for each of the years since 1966.

As for discounting the benefits of future regulations, I have not met anyone yet who would not spend $300-plus to receive a $900 return within ten years, especially since the $300 would be recouped within several years, assuming gasoline at 65¢ a gallon. And with the price of gasoline rising rapidly, the benefits far exceed these numbers. Although I agree that people discount future benefits differently, Rottenberg would need a discount of more than 30 percent to give value to his point.

In short, Mr. Rottenberg misses my key points: that producers who know how to make a product safer have an obligation to do so, and if they do not fulfill that obligation, then government must take it on because individuals cannot achieve the goal on their own. Unfortunately, Rottenberg, in his preoccupation with economics, passes over the fact that the sanctity of life has the highest value in our society.

Of Polls and Pollsters

TO THE EDITOR:

Some of the apparent inconsistencies in public attitude which were remarked on in "Perspectives" in the November/December 1978 issue may arise because of your treatment of the *U.S. News* poll as a public opinion poll in the same sense as a Harris or *New York Times* poll.

The sample surveyed by the *U.S. News* poll is not of the general public. It is deliberately chosen to represent potential subscribers to *U.S. News*. Consequently, it is more male, higher income, more conservative, and more strongly representative of management and executive personnel than is the general public. All this information is available in the publications distributed by *U.S. News* but is usually played down, neglected, or not aggressively and repeatedly mentioned in the narrative analysis with which they accompany the distribution of their results. Indeed, a superficial reading of their summaries and analysis would give one the impression that this was a true public opinion poll.

This is not to say that the *U.S. News* poll is without value. It is important to understand how even this higher income and more conservative group shares, to a large extent, much of the dissatisfaction with business and business performance that is exhibited by the general public. At the same time, it is also important, in the interest of understanding reality, not to uncritically ascribe the opinions of this special group to the general public.

You described some of the significant findings of the *U.S. News* poll, but did not note that these findings are even more dramatic given the nature of the *U.S. News* poll sample. For example, in this higher income and more conservative group

—72 percent believe that "monopoly is growing in the United States," and

—81 percent agree that "large companies have a major influence on government agencies regulating them."

These are the opinions of a group that is actually participating in business as middle management. They should, and probably do, know.

By treating the *U.S. News* poll as a public opinion poll, your analysis did not do justice to its real implications.

Eric A. Weiss,
Sun Company

THE EDITORS respond:

According to its published description, the 1977 *U.S. News* poll surveyed a sample of 13,012 heads of households drawn from Reuben H. Donnelly Corporation's lists of car-owning households and registered telephone households. Together these two lists comprise almost 65 million of the U.S. household total of 74.1 million. The survey was conducted for *U.S. News & World Report* by Marketing Concepts, Inc., was not identified with *U.S. News* in any way, and produced the good response rate of 51.6 percent. Although there was an initial oversampling of higher income groups so as to provide reliable data on these subcategories, the general results were weighted in order to eliminate this bias. In sum, the *U.S. News* poll is a survey of the heads of 65 million American households of all income levels, not "potential subscribers," and is just as much a poll of the general population as the Harris and the *New York Times* polls. ■

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Perspectives
on current developments

Blowing Bubbles at EPA

It has been vaunted as an "important experiment" and the "first major alternative to the . . . inflexibility" of traditional approaches to air pollution control (William Drayton, assistant administrator of the Environmental Protection Agency). It has been linked to "regulatory market strategies . . . designed to give both industries and local government marketplace incentives which will both speed up pollution reduction and lower its costs" (Barbara Blum, EPA deputy administrator). And it has been noted on the business pages of newspapers around the country as an indication of the Carter administration's new cost consciousness on regulatory policy. On closer inspection, however, EPA's new "bubble" policy, announced on December 21, appears to be a much less dramatic departure from old ways than the publicity suggests.

Under the 1970 Clean Air Act (as amended most recently in 1977) EPA is responsible for ensuring that each state enforces at least the "ambient air quality" (air pollution level) standards set out in the statute. The approach generally adopted in state implementation plans until now has been to specify precise limits on the amount of pollutants that may be discharged by each smoke stack, vent, port or other "stationary emission source" in an industrial or municipal plant. The "bubble" concept would instead set overall limits on pollutants (by various chemical categories) for an entire plant, allowing plant managers to determine the most appropriate mix of controls on individual emission sources within the plant. So long as the discharge level for a particular pollutant did not exceed the authorized level within this imaginary "bubble" over the whole plant, managers would be free, for example, to install additional (but relatively cheap) controls on some of their operations in order to reduce the need for costlier controls in another area. In principle, then, the "bubble" approach could allow substantial savings to industry without relaxing mandated reductions in air pollution.

While EPA's December statement marked the agency's first public endorsement of this approach, the agency's regulations have never forbidden it and some states have already negotiated similar arrangements with individual firms without objections from EPA. The statement was designed "to encourage [states] to consider" the bubble approach in the new round of state implementation plans which, under the 1977 Clean Air Act Amendments, must be submitted for EPA approval this spring. But the statement also sought to clarify the legal limitations on the bubble approach, and these turn out to be quite substantial.

The crucial limitation is that the bubble will essentially not be allowed for new plant construction. Under the 1977 amendments, areas that cannot show they will meet mandated ambient air standards by 1982 (which may turn out to include most of the country's larger cities) must require "the lowest achievable emission rate" from *every* emission source in *every* new facility. What is more, the amendments require new plants in the rest of the country to adopt the "best available control technology" for every emission source, a requirement that obviously allows far less flexibility than promised by the bubble concept. But EPA made no effort to dissuade Congress from enacting these rigid requirements in 1977, nor does it have any present plans to propose modifications to the new Congress.

The insistence on technology requirements for new construction has been characteristic of clean air legislation and EPA regulation from the beginning and the new "bubble" policy does not change it. It can be said in defense of the technology requirements that they help relieve regulators of the burden of determining the precise levels of "safe" or "acceptable" pol-

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lution for each kind of pollutant and that they ease the administrative burdens of enforcement. (It is obviously much simpler to check the installation and operation of required equipment on the ground than to carry out continuous monitoring of discharge levels in the air.) Significant as these advantages may be, however, they give little consideration to the costs involved.

In any event, the enforcement emphasis that underlies the technology requirements for new plants can be plainly discerned in the limitations EPA has announced for bubble arrangements within existing plants. The bubble will be available only to individual plants, because the discharge totals from a larger bubble (covering two or more neighboring plants, for example) would be harder to monitor. Moreover, a separate bubble will be required for each category of pollutant: there will, for example, be no trading of sulfur dioxide emissions for hydrocarbon emissions because the equivalents are too difficult for EPA to calculate. Nor will plants be permitted to trade readily measurable emission levels against emissions from less readily measured sources under the bubble. There is no question that EPA must take precautions to ensure that bubble plans do not actually wind up producing more pollution or more dangerous forms of pollution than the present system of individual source controls. But an extremely strict approach to trade-offs would significantly limit the cost-savings that are supposed to be the bubble's main attraction.

In fact, the seventeen-page statement of December 21 does not provide much detail about how these pollution trade-offs will be judged by EPA and the resulting ambiguities may—because of time pressures—limit use of the bubble approach still further. Under the 1977 Clean Air Act Amendments, states without implementation plans approved by July 1, 1979, will be forbidden to authorize any new construction and states may well fear dangerous delays in securing EPA approval if they misinterpret what can come in under the bubble. State regulatory agencies may thus find it safer and easier to refuse to consider bubble proposals from industry for the time being, as EPA officials privately concede. Unfortunately, while the states are free to propose changes in their implementation plans after the July deadline, plants must be held to the original scheduling of control requirements until changes are accepted—even if the company is drafting a bubble proposal for later on. There may be little time to develop the kind of imaginative engineering plans the bubble is supposed to encourage before such alternatives are preempted by the investments required under the original control schedule.

Plants with large and diverse operations (steel plants are a commonly noted example) may well be able to save substantial sums under the new policy, if they can apply sufficient pressure on state authorities for quick and sympathetic action. But it will be several years before the real impact of the policy can be assessed and much will depend on the degree of flexibility EPA displays in working out practical details. In the meantime, EPA may regard its endorsement of the bubble as a step toward "marketplace type incentives," but it seems fair to add that the step is neither swift nor sure—nor long.

The Sears Catalog of Litigation

Sears, Roebuck and Company, which annually pushes the equivalent of 1 percent of the GNP through its network of retail stores, is certainly accustomed to vast undertakings by now. But the suit launched by the company against ten federal agencies on January 24 is of staggering dimensions even for Sears.

Press accounts of the suit have focused on the fact that a successful outcome would forestall charges pending against the company in the Equal Employment Opportunity Commission. But this ambitious litigation certainly provides massive overkill if it is simply aimed at deflecting the EEOC charges. The complaint was prepared for Sears by Charles Morgan, former Washington national director of the American Civil Liberties Union and has, in fact, all the earmarks of the political suits we have come to expect from "public interest" law firms or traditional civil rights organizations—except that it is *more* ambitious in scope.

The charges voted by the EEOC in April 1977 were based on statistical disparities between the racial/ethnic/sexual composition of Sears's work force and what the commission

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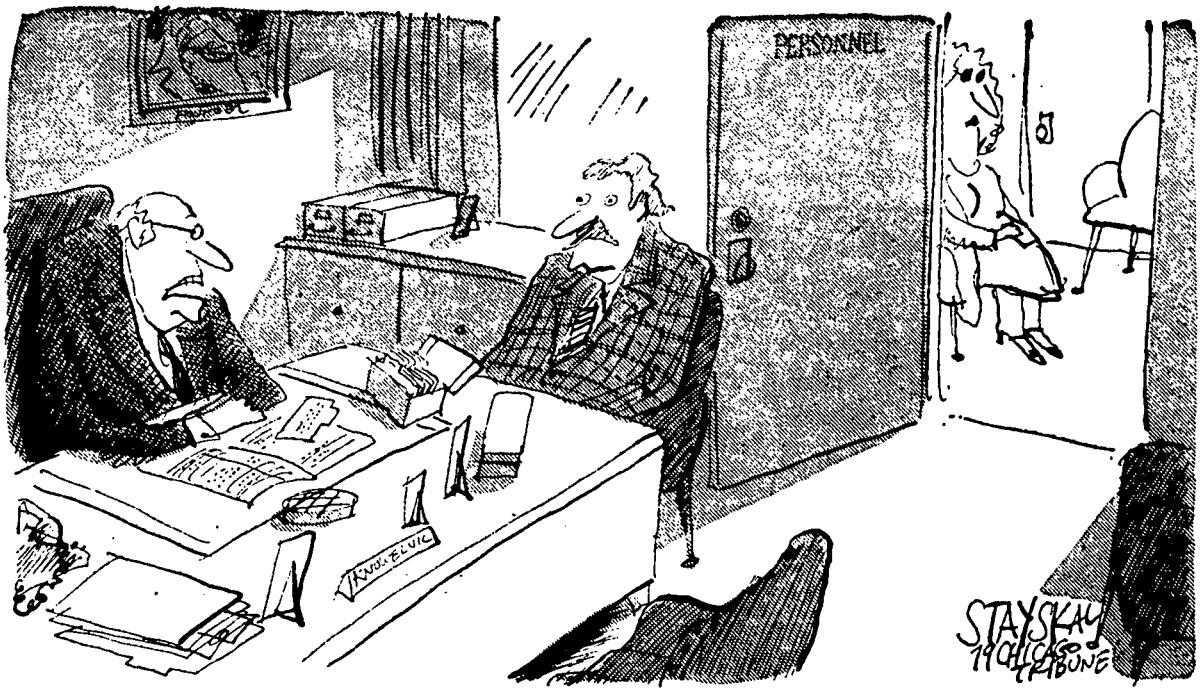

"You're well qualified for the job, Mr. Wimbish, but seeing our company doesn't discriminate by sex in hiring we're looking for a woman to fill it."

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judged to be the relevant categories in the national labor market. Sears argues that the EEOC has proceeded on the basis of unreliable or unrealistic statistics and, more important, that past action or inaction by the federal government itself has contributed to the underrepresentation of women and minorities in upper-level employment positions. Sears then requests a court order declaring that, "to the extent that government action or inaction created an unbalanced workforce," no federal agency should be allowed to use "statistical disparities to prove non-compliance with anti-discrimination statutes."

The audacity of the suit, though, is that it goes beyond seeking such restraint of the EEOC and requests a whole range of court orders against nine other federal agencies to bring about the circumstances which, in Sears's view, would make continuation of EEOC's statistical enforcement policies legitimate. Thus it requests an injunction requiring the Department of Commerce, the Bureau of the Census, and the Federal Agency Council on the 1980 Census to arrange among themselves to collect appropriate statistics "to enable Sears" and other retailers "to comply with the anti-discrimination statutes" by providing more reliable figures on the number of minorities and women at various levels of skill within reasonable commuting distance of a Sears store or facility. And it demands more vigorous enforcement of existing laws so as to make a more "balanced workforce" available to private employers. Specifically, Sears seeks court orders citing deficient or improper enforcement of:

—Title VI of the Civil Rights Act of 1964 (forbidding recipients of federal financial assistance, including schools and colleges, to practice discrimination on the basis of race or national origin),

—Title IX of the Education Amendments of 1972 (forbidding educational institutions receiving federal financial assistance from practicing discrimination on the basis of sex),

—Title VII of the Civil Rights Act of 1964 (banning racial or sexual discrimination in private employment),

—the Housing and Community Development Act of 1974,

—Title VII of the Civil Rights Act of 1968 (banning racial discrimination in housing),

—the Comprehensive Employment and Training Act,

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CATALOG OF COMPLAINTS

In the course of its thirty-two page formal complaint, Sears points a finger at numerous failings and irregularities in federal civil rights enforcement. Here are some of the background charges that did not find their way into Sears's particular requests for relief.

- Many federal agencies, including several charged with enforcing civil rights measures, have themselves been found guilty of race and sex discrimination. In 1976 alone, the Civil Service Commission issued 300 findings of employment discrimination involving federal departments and agencies. The chairman of the EEOC has stated that private employers "have been held to higher standards" than the federal government in nondiscrimination requirements.
- While the EEOC has charged the retail industry with employing a disproportionate number of women in part-time jobs, the percentage of women in part-time jobs is substantially higher in federal service jobs than at Sears or in private (nonagricultural) employment as a whole. In 1978 Congress actually enacted legislation *encouraging* federal agencies to increase part-time job opportunities, on the finding that, among other things, part-time employment "provides parents opportunities to balance family responsibilities with the need for additional income."
- In 1972 Congress established the Equal Employment Opportunity Coordinating Council to resolve conflicts and inconsistencies among the five agencies with primary civil rights responsibilities, whose heads would compose the council. Guidelines on Employee Selection Procedures were finally promulgated by the council in 1976, but two of the five agencies represented on the council refused to accept all provisions of the guidelines in their own policy statements and regulations. New Uniform Guidelines on Employee Selection Procedures were endorsed by four of the five agencies in 1978, but the uniform guidelines make no mention of present antidiscrimination statutes on behalf of the handicapped, disabled veterans, and the aged.
- The number of unresolved discrimination complaints pending before the EEOC rose from under 25,000 in 1970 to 130,000 in mid-1977. Internal audits of EEOC operations have pointed up destruction and falsification of files, employees performing work for which they had not been properly trained, and continuing friction between district and regional offices of the agency. Meanwhile, although government contractors have been required by executive order to take special "affirmative action" on behalf of minority employment ever since 1965, the agencies charged with enforcing this requirement have still not developed a reliable method for identifying companies that have government contracts. And a 1977 study found that the Department of Labor provided such inadequate guidance concerning the requirements of the 1963 Equal Pay Act that "it has effectively prevented employers from complying. . . ."
- The Bureau of the Census has admitted that the 1970 Census undercounted the total population, but undercounted blacks at a rate almost three times as high as whites and undercounted Hispanics at an unknown but even higher rate than blacks. The count of Hispanics was based on five different identification standards rather than a single, uniform definition.

—the Equal Pay Act of 1963,
—Executive Order 11,246 (requiring companies that have government contracts to take affirmative action to expand employment opportunities for women and minorities), and
—the Age Discrimination Act of 1975.

Sears does not specify what it wants the courts to do about this situation, although (as the company's complaint notes) courts have already imposed extensive procedural requirements on HEW's Office for Civil Rights in response to earlier suits charging inadequate enforcement. The complaint is even less clear about what it expects the court to do about its allegation that the preponderance of white males in upper-level positions in the economy, as at Sears, can be attributed in part to past government policies (notably the G.I. Bill of Rights, veterans preference laws and the selective service system, coupled with traditional restrictions on the number of women and

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blacks in the armed forces). The only specific request in this regard seeks an exemption for all retailers from the 1978 amendment to the Age Discrimination Act, so that employees may be forced to retire before age seventy to make room for minority hiring and promotion.

All of this adds up to an extremely tall order for the courts. The suit not only asks them to settle conflicts and ambiguities reaching to the highest level of national employment policy, but also invites them to make basic management decisions for more than half a dozen federal agencies. What this amounts to, in fact, is a plea for the courts to reduce what Sears considers the present chaos in federal regulation of employment practices to a coherent and effective enforcement operation.

Past judicial forays into detailed governmental administration (in cases dealing with schools, prisons, and hospitals, for example) have not been so well received that the courts can feel comfortable taking on the entire system of federal regulation of employment practices. If a more modest assessment of their own place in the scheme of things does not cause the courts to decline Sears's invitation to broad intervention, they may well be scared off in any case for the same reason that Congress and the executive branch have allowed so much conflict and confusion to accumulate in this area to begin with: it is a political minefield. Judicial intervention here will almost certainly engage political passions on the same scale as *Bakke*, with much less prospect of success. It is probable, therefore, that any relief the courts provide will focus upon protecting Sears from unrealistic hiring quotas, rather than upon eliminating government actions that contribute to making quotas unrealistic. Even this more narrow issue, however, may easily be avoided by a judicial determination that Sears has no "standing" to complain until some agency takes compulsory or punitive action against it.

Lawyers for Sears have insisted that a complete vindication of their claims would eventually bring great benefits to minorities and women, even if it temporarily disrupts the operations of the EEOC. They argue that the suit should actually make the government's performance more acceptable both to business and to civil rights activists. That may well be. It will still leave the government's performance unacceptable, however, to individuals such as Allan Bakke and Brian Weber who claim to be the casualties of government-imposed or government-induced affirmative action quotas. In placing the Sears case within the context of the current minority-employment controversy, the most significant factor is that Sears, like the other institutions involved in the recent landmark cases—the University of California in *Bakke*, and Kaiser Aluminum in *Weber*—is defending the quota system. Its pleas for relief include a court order shielding its present system of hiring quotas from "reverse discrimination" suits. Indeed, its entire complaint can be regarded as a plea for such changes in the government's policies and practices as are necessary to enable the quota system to work.

Sears has at least performed a valuable service in highlighting the disarray in federal civil rights and employment regulation (see box). It remains to be seen whether the wider public service that this ambitious suit seeks to perform will be accomplished or—if accomplished—welcomed. And one may wonder whether the courts are really the appropriate arena in which to carry on such public service activities.

Sour Lemons at the FTC

The Federal Trade Commission's newest monopoly decision illustrates an old problem and raises some new concerns. The old problem is time—how relevant is a decision based on facts over four years old? The new concern is the FTC's notion that monopolists should not be allowed to engage in price competition.

In July 1974, the FTC charged Borden with "unlawfully maintaining monopoly power . . . in the production, distribution and sale of reconstituted lemon juice," through sales of its ReaLemon brand. Hearings began almost a year later and continued—off and on—until February 1976. On August 19, 1976, an administrative law judge held against Borden and ordered what many viewed as drastic relief—that the ReaLemon trademark be licensed to all comers for the next ten years. More than two years later, on November 7, 1978, the FTC agreed that Borden had violated the antitrust laws but found the proposed remedy "unnecessary." Instead, the commission enjoined Borden from a

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variety of specific activities, including charging "unreasonably low prices."

From the beginning, this was a strange case. The processed lemon juice market (finally determined to be the appropriate relevant market) was very small, with only about $25 million in total sales, thus making it an unusual target for concern about monopoly. In addition, while ReaLemon was the first product of its kind and had (presumably as a result) dominated the market since its introduction in the 1930s, its market share had fallen rapidly in the years immediately preceding the FTC's original complaint—roughly from 89 percent in 1969 to 75 percent in 1974. The primary complainant itself had made significant inroads—acquiring approximately 15 percent of the national market in only four years—even though it "routinely" (according to the FTC) adulterated its product. In addition, in the two years between the administrative law judge's decision and the FTC's final opinion, Minute Maid (a subsidiary of Coca Cola) introduced a wholly new variant —frozen fresh lemon juice—and acquired over 8 percent of the national market.

Thus, by the time the FTC concluded that Borden's "continued domination of the market" was the result of "manipulation . . . of a strong consumer franchise . . . that enabled it to exert a 'magnetic pull' on the consumer," Borden was already fighting a stiff commercial battle against a price-cutting competitor and an innovative new entrant, neither of whom were apparently aware that Borden had "the power to control prices or exclude competition."

The FTC based its findings of monopoly power not so much on Borden's market share as on its trademark. The ReaLemon mark, said the FTC, had become so well known and accepted that it gave Borden an unfair advantage over other actual and potential competitors. Because the trademark was so well known, Borden could charge higher prices than its competitors. When new competition appeared, Borden thus had the power to respond with a substantial price cut. Since any other brand would have to sell for substantially less than ReaLemon in order to compete with the trademark, the new competitor would have to lower price below cost and eventually go out of business. This process, said the FTC, allowed Borden to exclude equally efficient competitors simply because they did not have the advantage of a well-known trademark.

In the context of this analytical framework, the FTC found Borden guilty of "selective price cuts . . . aimed at reducing the price spread between Borden and its competitors . . . with the specific intent of recapturing market share. . . ." In other words, to the FTC, Borden's monopoly market share was not "economically inevitable" since Borden was under no compulsion to respond to new competition. Borden had thus maintained its monopoly, and in so doing, violated the law.

The FTC has been a strong supporter of legislation to create a new, "no-fault" monopoly offense, eliminating the "bad conduct" requirement in the current law. If the commission's decision in this case stands on appeal, there will be little need for such legislation, since the Federal Trade Commission Act will for all practical purposes already include the offense. After all, the FTC charged Borden not with *creating* an unlawful monopoly, but merely with unlawfully *maintaining* a (presumably legally obtained) monopoly. And it did not charge that any of Borden's actions, standing alone, was illegal or that Borden's conduct was "bad" in any normal sense of the word.

This opinion is bound to fuel the sort of charges that led the *Washington Post* to label the FTC our "National Nanny." FTC Chairman Pertschuk, for example, pointed out that consumers are obviously confused "to the extent that [they] perceive ReaLemon to be objectively superior to other brands. . . ." The fact that people prefer ReaLemon was traced by the commission to "spurious product differentiation" that exerts a "magnetic pull on the consumer." No one mentioned the possibility—despite the adulteration by ReaLemon's leading competitor—that people might know and trust the ReaLemon brand and be willing to pay a few cents more on an infrequent purchase for this familiarity and reliability.

Some have questioned whether the FTC, in this opinion, is protecting competition—or competitors. Its order enjoined Borden from (1) charging different prices in different regions of the country and (2) selling at "unreasonably low prices." The first injunction will make it more difficult for Borden to respond to local or regional competition. If Borden wants to lower price in Philadelphia in response

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In Brief–

Ungoofing. It is common for critics to charge that Congress imposes costly new regulatory requirements before really considering their need. It is less common for Congress to respond in time to avoid the damage. But that is what Congress has done in repealing a particularly costly section of the Right to Financial Privacy Act of 1978.

Section 1104(d) of the act required all financial institutions to notify *all* their customers of all their rights of recourse in case a government authority should ask the institution for the customer's records. The notification was to take place not when there was such a request but "promptly" upon the act's becoming effective (March 10, 1979).

The banking industry estimated it would cost $922 million to carry out the requirements of section 1104(d), more than half of that ($515 million) being for manual retrieval of inactive accounts. Pressure was put on the Congress to retrieve the situation before the act went into effect. Curiously, the legislative history of the bill does not mention the offending provision, so it is hard to say why Congress thought it was needed in the first place. But the significance of the repeal, passed by both houses this February, is clear enough. The repeal is, as Republican Thomas Evans of Delaware put it, to be "the first in a long series of measures which will remove costly and unnecessary federal requirements."

Customers will be notified of their rights of recourse when the government wants to look, is looking, or (in the case of a search warrant) has looked at their records, but there will be no blanket notification. The banking industry will be spared the expense of retrieving dead accounts. And Congress will have saved itself a scolding on at least one goof.

Snail Darter Lives On! When last heard from in these pages, the snail darter was holding its own against the multi-million dollar dam that threatened its "critical habitat" (see *Regulation*, January/February). Now the three-inch fish has triumphed for good.

Readers will recall that the Supreme Court barred completion of the Tellico Dam on a literal reading of the Endangered Species Act, and that the Congress reacted by authorizing a cabinet-level Endangered Species Committee to grant exemptions to the rigid provisions of the act. Meeting on January 23, the committee voted unanimously against exempting the Tellico Dam. It not only found that alternatives to the dam were feasible but also that one alternative would be more cost effective than completing the dam.

It was lucky for the snail darter. The staff report prepared for the committee by the Interior Department strained without much success to establish a larger significance for the tiny fish. "Knowledge of the snail darter's highly selective food habits and habitat choice makes the species interesting and gives esthetic pleasure to some people," observed the report. With an equally straight face, it offered a plea for the darter's historical value: "We can assume that the present controversy will eventually have significant historical value. Some of this value may accrue to a preserved snail darter by virtue of the species central role in the controversy."

Too Much Civic Spirit? The Federal Trade Commission is considering a rule that would require used-car dealers to notify customers of the mechanical deficiencies in each car sold. According to the commission's staff, consumers generally cannot judge engine condition and frequently wind up making purchase decisions on the basis of more visible but less reliable indications of value, like body condition. The staff report makes a credible case that the disclosure requirements would correct for this market imperfection at little cost, allowing consumers to pay for engine quality, not surface glitter.

But the report embellishes its case with an argument that may distress advocates of corporate social responsibility. It seems that car buyers often rely on a dealer's reputation. Not content with pointing out that reputations may be misleading indicators of car values, the report warns that "reliance on reputation can lead to resource misallocation. Dealers who might otherwise invest more in vehicle quality or lower prices instead must compete in 'reputation.' Thus, for example, numerous dealers who testified at the hearings made a point to list their extensive involvement in civic affairs." Presumably the FTC's used-car rule would avoid this waste. Whoever said the FTC was too fascinated by fuzzy-headed "social considerations" to take a hard view of the requirements for competition?

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to localized competition there, it will have to lower price everywhere unless it can show that the different price is cost-justified, not just competition-justified. This can be expected to discourage Borden from lowering price anywhere. The second injunction will offset the power of the trademark and limit *all* responses to new competition—as Commissioner Pitofsky put it—to a "restrained and moderate price cut . . . perhaps down to average full cost, since this would give the challenger time to become established in the market, at which time the two could fight it out on the merits."

While it is not at all clear what the FTC means by "fight it out on the merits," it certainly means bad news for consumers. Any rule that prohibits a response to competitive price-cutting inevitably means higher prices. Borden's

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new bureaucratic straitjacket prevents it from fighting anything out with inefficient producers, who will be allowed to gain market share until Borden is no longer a monopolist. By then Borden will presumably be free to reduce its price closer to marginal cost and regain its market share, thereby (eventually) benefiting the long-suffering consumer. The FTC has taken what appears to be a competitive monopolist and turned it into an "easy life" monopolist by requiring it to hold a pricing umbrella over inefficient competitors. In the process, the FTC has taken onto itself the job of deciding what prices are "reasonable" in the processed lemon juice market—the kind of thing it continually urges the Interstate Commerce Commission and other regulatory agencies to stop doing, and the kind of thing the Supreme Court has consistently declined to do on the grounds that it is impossible.

If this is an example of the kind of result that a "no-fault" monopoly statute would produce, such a statute would indeed be against the consumers' best interests. If using a trademark is monopolistic—if building up brand loyalty can be deemed contrary to consumer interests—then any process by which consumers are informed can be challenged. When the FTC decides that it knows best for consumers (even in the absence of fraud or deception) simply because it is more sophisticated, and is able to enforce its prescriptions under an antitrust banner, we have moved a very long way indeed from Senator Sherman—and certainly not in the right direction.

No Confidence in Old Trusts

The National Commission for the Review of Antitrust Laws and Procedures, which issued its final report to President Carter and Attorney General Bell on January 24, 1979, may prove to have more impact on federal regulatory reform than anyone anticipated when the panel was assembled last June. The bulk of the report is taken up with recommendations for improving antitrust trial procedures and for amending the Sherman Antitrust Act to help speed up "big cases" like the Justice Department's action against IBM, now in its eleventh year. (See Sims, "The President's Commission on Antitrust," page 25.) But the report also devotes considerable attention to the possibility of removing antitrust exemptions from several regulated industries—thus allowing the clumsy and ineffectual regulatory structures in these industries to be removed at the same time. Its recommendations would in any case allow the Justice Department to enforce true competition in industries where, with the help of government regulation, it has often been notably lacking.

The commission was drawn into these questions of regulatory policy through one element of its original charge—that it examine "the desirability of retaining the various exemptions and immunities from the antitrust laws. . . ." Because most of these exemptions are connected with larger regulatory schemes —usually putting the particular industry under the tutelage of a specialized regulatory agency —the commission quite early decided it would have to consider the "entire economic regulatory system" in each case in order to evaluate the antitrust immunity involved. It examined five industries and relied heavily on previous critiques of these regulatory programs, notably the Ford Administration's Task Force on Antitrust Immunities (which issued extensive reports on three of the five industries in 1975). The commission's findings are not startlingly new, but the prestige of its membership (which included key members of Congress, high regulatory officials in the Carter administration, and legal scholars and practitioners) and their near unanimity on most points should give a significant new impetus to the reform proposals.

Surface transportation. The report's recommendations here were the most sweeping. They urge a total dismantling of the Interstate Commerce Commission's regulation of trucking, and unconditional repeal of the antitrust immunity for joint rate-setting by truckers and by railroads provided in the Reed-Bulwinkle Act of 1949. In expressing general sympathy for deregulation of railroads, however, the report does include some caveats about the risks of wholesale abandonment of existing lines in a completely unregulated environment.

Insurance. Much state regulation of insurance is made possible by the antitrust exemp-

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tion for the insurance industry contained in the 1949 McCarran-Ferguson Act. Here the commission's report goes even further than the Ford task force (which had proposed consideration of an alternative federal regulatory scheme). The commission found "a general consensus that most segments of the industry are competitively structured" and therefore that existing state regulations simply increase costs. The report acknowledges the concerns expressed by some commission members that a free market in insurance might put onerous burdens on those least able to pay and most in need of insurance. But it does not go beyond suggesting further study of this problem, and its recommendation for repeal of existing antitrust exemptions is plainly premised on the emergence of an essentially free market in insurance. The report does, however, note the need for a statute "affirming the lawfulness of a limited number of essential collective activities" relating to data collection and computation of actuarial statistics.

Agriculture. With surprisingly little controversy, the commission concluded that the 1922 Capper-Volstead Act's antitrust exemption for agricultural cooperatives is not adequately balanced by the secretary of agriculture's present authority to act against "undue price enhancement"—an authority that has never once been exercised. The report urges (with only one dissent) that cooperatives should generally be subject to antitrust constraints but that their initial formation not be considered a per se violation of the antitrust laws. This would allow small farmers to pool their output for marketing purposes while prohibiting cooperative mergers or intercooperative agreements when their effect may be a substantial lessening of competition in some relevant market. For all its obvious appeal, this compromise may be difficult to express in effective legislative language or to enforce in practice.

Ocean shipping. The commission recognized the large economic costs imposed by the present regulatory framework in this area—essentially self-regulation by carriers with loose oversight by the Federal Maritime Commission. The report does not quite call for wholesale antitrust action against the existing system of shipping conferences (which establish common rate structures among shipping companies with parallel routes). But the commission did express considerable doubt about the two principal arguments for the conference system: that international comity considerations preclude the United States from unilaterally changing its regulatory policy and that national defense considerations require protection of U.S. flag carriers from low-cost competition. The commission had no hesitation, at any rate, in recommending that the existing antitrust immunities provided in the Shipping Act of 1916 ought to be significantly narrowed (as the Ford task force had earlier recommended). For one thing, its report urges that conferences be restrained from efforts to prevent independent action by member companies. The report also recommends that conferences be forbidden from entering dual rate agreements, rate agreements with independent lines, or pooling agreements with other conferences.

Export associations. The report asks Congress to rethink the desirability of the Webb-Pomerene Act of 1918, which provides antitrust exemption for export associations. The commission took this position despite warnings from the Commerce Department and the commission's own business advisory panel that enforcement of antitrust laws could hamper U.S. companies in international competition. Acknowledging these concerns, the commission did not urge outright repeal of the present exemption but did recommend that Congress narrow the antitrust immunity of export associations by making it contingent on a showing of need in each situation.

The proposed Competition Improvements Act. The commission endorsed the competition improvements bill proposed by Senator Kennedy and introduced in the last Congress as S. 2625. The measure would require regulatory agencies to study each new decision's potential effects on competition and to ensure that decisions are structured to keep burdens on free competition to a minimum. Though the proposal has been around for some time, it has been held up by concern that it would increase the cost and delay of regulatory decision-making, as the requirement for environmental impact statements has done.

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Viewpoint

Needs and Licenses

Michael Pertschuk

OUR CULTURE is dominated by professionals who call us clients and tell us of our needs. Morticians advise us of what is required for a decent burial. Sex therapists counsel us about what is required for intimacy. Professional hypertrichologists diagnose and treat our "excessive and unsightly" facial hair. Our children's education requirements are determined by professional teams of speech therapists, learning disability specialists, child psychologists, social workers, school administrators, and guidance counselors.

Our very language has transformed the word "need" from a personal verb, dependent for its content on the one who feels it, into an objective noun. Needs are now somehow separate and apart from people; they have become the objects of professional competence, beyond our private competence to diagnose. We speak of the "delivery" of health care or social services and of the "achievement" of mental health or degrees of educational competence as if we were talking about commodities manufactured in uniform portions for those who lack them.

The increasing ubiquity of the professionals has had an insidious and intimidating effect. We lack confidence in our unprofessional abilities to diagnose our private needs on the basis of our personal experience. Increasingly, we ask professionals to reveal our needs, not merely to service them. The professional stockbroker, real estate agent, insurance agent, doctor, dentist, lawyer, pharmacist, auto mechanic, architect, interior decorator, psychiatrist, mortician, family planner, organizational development specialist—all now counsel us about our needs, advise us about what we should want, and then service their own prescriptions.

This combination of diagnosis and service is often efficient—how wasteful it would be to require that the diagnosing physician or auto mechanic put the body back together again before offering to repair it—but it is also open to subtle abuse. How can the diagnostician be relied on to understand our unique preferences, our own particular willingness to trade quality against price, our unique aversion to risk? And since it is difficult or impossible for us to know whether the recommended services match our personal preferences, how can the diagnostician be relied on not to try to maximize his profits simply by recommending services that will bring him the greatest gain?

To the extent that diagnosticians are conscientous, relying on time-consuming personal interviews and making the effort to listen and explain, they are apt to earn less than they could by sending us off to costly diagnostic centers filled with complex equipment for analyzing our physical, psychological, emotional, or financial needs. And to the extent that diagnosticians prescribe changes in personal habits or routines they are likely to earn less than they could by applying the techniques and remedies for which they have been trained and on which they profit. As a result, we are liable to misdiagnosis and overprescription.

It is estimated that 33 cents of every dollar spent last year on auto repair went for unnecessary work. It is also estimated that 2 million Americans underwent operations last year they did not need, at a cost of 10,000 lives and $4 billion. And personal expenditures for lawyers, physicians, dentists, and other professionals are increasing at a rate faster than the average for all goods and services in the economy.

Ironically, licensing is both a response to, and a cause of, this problem. It is a response because—theoretically—it brings to bear the government's comparative advantage in policing against misleading diagnoses and excessive service. If consumers are unable to evaluate bundles of diagnosis and service, then arguably the government should step in and set minimum standards to ensure the competence and

This essay is drawn from remarks by FTC Chairman Pertschuk at AEI's Conference on Occupational Licensure and Regulation, February 22, 1979.

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integrity of those who offer such bundles. Variations on this argument are sounded to justify most licensing schemes. Indeed, some concerned consumer groups now urge that auto mechanics be licensed in states where they are not, and that the licensing of lawyers and physicians be made stricter in order to guard against the kind of shoddy service that spurs dramatic increases in malpractice suits.

But licensing is also a cause of misdiagnosis and overprescription to the extent that it becomes a vehicle for a profession's legitimizing its monopoly on discovering and remedying needs, and enforcing its mystique by limiting access to special knowledge. Generally it is the members of a particular occupation—not the public—that seek licensing (as a means of enhancing prestige and income). At a recent session of one state legislature, occupational groups advanced bills to license themselves as auctioneers, well diggers, home-improvement contractors, pet groomers, electrologists, sex therapists, data processors, appraisers, and TV repairers. Hawaii licenses tattoo artists. New Hampshire licenses lightning-rod salespeople.

The evolution of certain occupations from being collections of individual sellers to tradesmen to certified professionals and, ultimately, to licensed professionals is well known. Barbers have been transformed into cosmetologists, garbage collectors into sanitary engineers, undertakers into grief counselors. Specialized courses of study are required, displacing apprenticeship and on-the-job training. Qualifying exams, citizenship and residency requirements, and professional fees are imposed on new entrants. Professional journals appear, Washington offices are opened to lobby for favorable legislation, and public relations firms are retained to ensure a favorable image. The profession develops status, political strength, and exclusivity. And each of these attributes reinforces the others.

It is hardly surprising that, once licensed, a profession is in a position to determine how much competition it will tolerate. Licensing boards dominated by members of the profession may act like any other cartel—adjusting entry standards to protect the incomes of established practitioners. It is not unusual for boards to reject higher percentages of applicants during periods of economic downturn when there is less demand for their services. Nor is it unusual for these boards to restrict advertising, promotion, and innovative ways of providing services, thereby making it more difficult for new entrants to compete.

Thus, like members of medieval guilds, the licensed professionals can maintain their privileged positions regardless of market forces. Study after study has shown that licensing results in higher direct costs to consumers and that indirect costs, in the form of foregone innovation and experimentation, are higher still.

But what about quality? Higher prices might be justified if quality were improved, if there were fewer cases of misdiagnosis and excessive service. Unfortunately, the fact is that all too often licensing bears little relationship to quality. Several years ago the Federal Trade Commission (FTC) compared the price and quality of TV repairs in Louisiana, where repairers were licensed, and in the District of Columbia, where no licensing was required. The result: prices were 20 percent higher in Louisiana and the incidence of unnecessary repairs was virtually the same in both places. Other studies show that uncontested divorces result in the same incidence of legal error whether handled by the parties themselves or by lawyers, and that clinical labs licensed by states have the same incidence of inaccurate clinical test reports as the unlicensed labs.

Indeed, licensing boards rarely monitor quality. Most professionals, once licensed, are licensed for life. One needs periodic reexaminations in most states to drive a car or pilot an airplane, but not to continue practicing as doctor or lawyer. From 1967 to 1973, the number of doctors disciplined by state boards for incompetence averaged only 1.6 per state, per year.

When licensing renders certain services unavailable to those segments of the population that cannot afford to pay for licensed professionals, consumers can end up with poor and dangerous quality of the do-it-yourself variety. One study, for example, shows that states with the most restrictive systems for licensing electricians also have the highest rates of deaths from accidental electrocution.

Are we bound, then, to a closed circle of professionals who identify and adjudicate our needs, professionals admitted to practice by professionals and policed by the same professionals? I do not think so—for a rebellion is brewing. Blame it on a revival of populism, on

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a resurgence of frontier self-sufficiency, on two decades of economic analysis focusing on occupational licensing, or on increased skepticism about government. Whatever its cause, the barriers to entry and innovation erected by professionals are beginning to fall.

The Supreme Court has struck down state laws prohibiting price advertising by pharmacists and lawyers for routine goods and services —laws passed at the behest of the professionals. Last year the Federal Trade Commission lifted restrictions on price advertising by optometrists, opticians, and ophthalmologists. More recently the commission issued a consent order that bars the American Society of Anesthesiologists from deterring its members from working under contract with hospitals. The FTC staff has recommended a rule requiring funeral directors to disclose the full range of their prices and options. And it is investigating physician control over Blue Shield boards, as well as licensing practices among lawyers, accountants, and dentists.

Private groups and many of the states have also taken steps to open up the professional marketplace. The American Veterinarian Medical Association and the American Psychological Association, after discussions with the FTC, have revised their codes of ethics to permit members to advertise. A committee of the American Bar Association has proposed streamlining ABA disciplinary procedures. California has placed a majority of public members on most of its licensing boards. Twenty-three states have enacted some form of sunset legislation to enable them to watch over their licensing boards. In Minnesota, no group can submit proposed licensing legislation without satisfying the state's Legislative Audit Commission that licensing is necessary.

More and more consumers are discovering that professionals are not markedly different from other sellers who offer their services in trade. Nothing dissolves a mystique faster than seeing lawyers advertise inexpensive legal services just as used-car dealers advertise special deals. Making visible the commercial underpinnings of the professions is therapeutic. It fosters healthy skepticism, and it teaches that, in this area as in all other commerce, vigorous competition coupled with adequate consumer information ensures the optimum range of quality at the lowest possible price.

Certainly it is necessary to be concerned about fraud and deception in these professions, just as it is with door-to-door sellers. But there are means of guarding against fraud and deception that are far less restrictive than licensing. Certification is one alternative. It provides consumers with information about the competence of the seller without creating a barrier to entry. Separation of diagnosis from service —the "second opinion" that allows consumers to do comparison shopping—is another alternative (which is why the FTC eyeglass rule requires eye examiners to provide consumers with a copy of their prescription).

The Federal Trade Commission is committed to finding and remedying vestigial and unjustifiable restrictions on the market for professional services. The remedying is the more difficult part, of course. FTC rulemaking is a less attractive approach than cooperation with state and local officials and concerned citizen groups—less attractive in part because the FTC may be less equipped than state and local officials to undertake the difficult trade-offs that are often involved. One area where the FTC can act without arousing substantial concern—indeed, an area where the commission has a major role to play—is in the provision of information, designing and funding studies that compare the effects of alternative regulatory systems on price and quality and serving as a clearinghouse for the findings of other studies.

At the same time, the FTC must carry out its congressional mandate to police unfair methods of competition and unfair and deceptive practices in the marketplace. And it will continue to act forcefully where professional regulation violates the basic tenets of our laws of competition and consumer protection and where there exists no serious alternative reform possibility.

When enough barriers have been removed so that professionals, disciplined by the market, must rely to a greater extent on their reputations for competence; perhaps then we consumers will be more confident of ourselves and less awed by those who tell us of our needs. We will bury the unfair advantages of the morticians, retreat from the intimate queries of the sex therapists, discover that hypertrichologists are excessive (if not unsightly), and require that the teams of educators do in fact educate our kids. ■

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RUMINATIONS ON A RAT: SACCHARIN AND HUMAN RISK

William R. Havender

THE HUBBUB began in earnest when Canadian scientists claimed in 1977 that saccharin caused cancer in rats and the Food and Drug Administration, invoking the Delaney amendment, then proposed to ban the use of saccharin in foods and soft drinks. This evoked a vociferous public protest, and Congress, swamped with angry letters, voted an eighteen-month moratorium on the proposed ban to allow the National Academy of Sciences to complete its own evaluation of saccharin's risks and benefits. That evaluation is now in hand, and the moratorium ends in May, so Congress will shortly have to make its final decision. It is thus timely to see what we know about the benefactions and malefactions of saccharin, and what these imply for shaping a wise regulatory policy. We are venturing, of course, upon dark and bloody ground where battles have raged, but we will emerge with quite firm conclusions about the form that responsive regulation ought to take.

Does saccharin cause cancer in rats? The answer is doubtlessly yes, since this has been shown in three independent experiments. But the effect was always weak and could only be demonstrated at the limit of these tests' sensitivity. There is little dispute over these facts, but the consensus evaporates altogether over the problem of extrapolating human risks from rodent tests.

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Of Rats and Men

Let us take a brief look at the experiments. It is customary to use whopping doses of a suspect substance in animal cancer tests, because there are financial and logistical limits to the number of animals that can be used in any single test. A typical test for a suspected carcinogen (cancer-causing substance), for example, might consist of 50 animals of each sex exposed to each of two different doses of the substance, with 50 undosed animals of each sex for comparison (300 animals in all). This would cost more than $250,000 and would last not less than four years (the two-year lifetime of the animals, plus the time for the preparatory experiments to determine dosage, plus the time for a pathologist to examine the microscope slides from some *forty* different tissues from *each* animal for signs of cancer). But the smallest number of tumor-bearing animals

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that could be detected in such a test (assuming we detect any) would be one animal at the highest dose, or only 1 percent. An incidence of 1 percent in a population of 200 million persons is 2 million cases; that is, a substance capable of causing some 2 million cases of cancer in the United States might well go undetected if it were tested only at doses that simulated human usage. However, since the number of tumorous animals will usually increase as the dose of a carcinogen increases, the test's sensitivity can be magnified by using very high doses. And in fact, the normal practice is to include the highest dose that will not poison the animals to death (the maximum tolerated dose, or MTD) in order to make the test as sensitive as possible.

It is this practice that has engendered public impatience with the saccharin tests, since the rats developing tumors had been fed the equivalent of 800 diet sodas every day of their lives. FDA spokesmen have tried to soften this impatience by explaining what I have explained here—that there *is* a valid reason why such doses are employed and that feasible experiments in the dose range of human usage would not be sensitive enough to detect agents that might still cause numerous cases of cancer. Nevertheless, there *is*, too, a valid question at the core of the public's skepticism about such enormous doses—namely, can things happen at such high doses that do not happen at all, or at least not in proportion, at the low doses typical of human usage? This is a profound rather than naive question, and the short answer is that no one knows and there is no simple way to find out.

When considering the three critical saccharin tests, one is made uneasy, however, by the fact that tumors were observed only in the rats receiving the highest dose (MTD). While these animals had normal life spans,* they were still clearly suffering metabolic distress, as shown by the fact that they had lower weights or smaller weight gains (between 10 and 20 percent less, on the average) than their undosed counterparts. This introduces a tinge of doubt in interpreting these results, because the observed tumors could well be a side-effect of metabolic stress that would not develop at all in the absence of debilitation. In any case, weakened animals might be more susceptible to cancer than healthy ones, so that *quantitative* extrapolations of risk to humans (that is, attempts at estimating the number of cancer cases expected in humans from the numbers seen in rats) are made somewhat dubious.

Two other features of these experiments also bring human risk estimates into question. One is that tumors have, with a single exception, been observed only in tests that lasted for *two* successive generations. Thus, most of the animals developing tumors had not merely been fed saccharin from the time they were weaned but had in addition been conceived, gestated, and suckled by mothers whose own tissues had been saturated with saccharin. Since fetal tissues are generally much more sensitive to injury than adult tissues (recall thalidomide!), it is primarily this exposure during a supersensitive stage that leads to cancer. This view is supported by the fact that no cancers were seen in five out of six *one*-generation rat-feeding tests (where saccharin doses started only at weaning), nor in two similar tests in mice. This fact—that animals exposed to saccharin *in utero* are far more susceptible to cancer than those exposed only after weaning—adds further uncertainty to risk estimates for human *adults* made from animals thus exposed. Perhaps the easiest way to see this is to realize that the sensitivity of fetally exposed rats would not predict the cancer rate even among *rat* adults that had been exposed only since weaning!

Finally, only the *males* developed tumors in all three rat tests, not the females. Such sex differences are not uncommon, but in this context they mean that male rats could not be used to predict the risk even for females of the same strain raised under identical conditions—thus further weakening the reliability of estimates of human risk.

These uncertainties are, of course, superimposed upon the more general uncertainties involved in all animal cancer tests. One of these is: do rats metabolize saccharin the same way humans do (at least when corrected for differences in body size and lifetime), or are they perhaps special in some pertinent way? We do not know; rats could be less, more, or as sensi-

*It is noteworthy that the animals did *not* die prematurely from the tumors. The induced tumors were described in all cases as "of low invasiveness" with "no reported metastases." Thus, saccharin induces only a very weak form of cancer in rats.

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tive as humans. Scientists assume for simplicity that there are no important differences in metabolism, but this is merely a convenience, not an unassailable fact.

Nor are we sure how to estimate the risk at low dose from determinations made at high dose. The usual procedure is to assume that the low dose risk is simply proportional to the decrease in dose, but no one knows if this is true over the entire thousandfold range from the MTD to the levels of human use. However, the assumption is fundamental to quantitative risk estimates, and in particular to answering the question whether there exists a "safe dose," or "threshold." Although the described limitations of animal tests prevent us from answering this question directly, we can specify certain requirements that would have to be met for the response at low dose to be proportional. One is that the organs and processes that clear saccharin from the body must function as efficiently at near-lethal doses as at doses a thousand times lower. (If, for example, they became overloaded at high dose and were less effective at removing saccharin, then the assumption of proportionality would *over*estimate the true risk at low dose.) The same restriction—no overloading at high dose—must hold as well for any biochemical mechanisms that might repair the chemical damage caused by saccharin (such repair processes are quite common for other kinds of chemical damage that lead to cancer). We have no evidence that these conditions are *not* met, but it is merely supposition —not established fact—that they are. And because we are extrapolating over a large dose range, even a small inaccuracy in our assumptions would reduce the cancer incidence at low dose appreciably below what it would be if the reduction in risk were proportionate to the reduction in dose.

Another complicating factor is that the length of time that passes between first exposure and the appearance of an induced cancer (called the latent period) may itself depend upon dose, being longer at low dose than at high dose. Since the rat cancers developed late in the life of the animals, only a small increase in the latent period at low dose would result in the animals' dying first of ordinary old age. We could thus define a "practical" safe dose as the one at which the latent period exceeded the life span of the animals. We have no evidence for or against such an effect with saccharin, and the evidence for such a process with other carcinogens is disputed. But again, only a small effect of this type would lead, given the thousandfold dose reduction, to a large decrease below proportionality in the cancer incidence at low doses.

The final problem in making low dose predictions arises because laboratory animals are bred to be *uniform* in their genetic sensitivities, whereas human populations have enormous genetic *diversity*—which means there is probably a great variety in human susceptibilities to any carcinogen. The incidence of cancer in such a varied group could not decrease simply in proportion to the decrease in the dose, because not *only* is the dose declining, but so also is the *segment* of the population that is sensitive to it. Thus, the incidence at low dose must be lower than would be predicted by assuming a reduction in incidence proportional to the reduction in dose. And since we are talking about a thousandfold decrease in dose, this effect is probably not negligible. (Only one of the various methods of dose extrapolation—the Mantel-Bryan probit model—takes this natural variation in sensitivity into account.)

In sum, then, there seems little reason to doubt that rats can indeed be made to develop tumors in response to saccharin, when we stand on tiptoe to do it. But saccharin is an extremely weak carcinogen—it is "among the weakest carcinogens ever detected in rats," as the Office of Technology Assessment put it. Also, quite precarious assumptions are entailed in estimating the probable cancer incidence in humans. Specifically, it is simultaneously assumed that

(1) visibly toxified animals have the same susceptibility as healthy ones, *and* that

(2) the sensitivity of animals exposed *in utero* is the same as animals exposed only after weaning, *and* that

(3) no unanticipated metabolic differences exist between rats and humans—and, in particular, that the susceptibility of male rats, though clearly different from that of female rats, is nonetheless the same as human adults (including women), *and* that

(4) the chemical effect of saccharin and the rats' physiological response is the same over the entire relevant dose range, *and* that

(5) there is no change in the latent period when doses are changed, *and* that

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(6) human populations have no greater genetic diversity in saccharin sensitivity than inbred rats.

Given these assumptions, the calculation of human risk from the rat data is quite straightforward. The resulting numbers range (depending on the particular body size, dose, and lifetime corrections employed) from less than a dozen cases of bladder cancer per year to at most a few thousand, with most estimates falling near several hundred cases per year. (Bladder cancer was the only kind seen in significant numbers in rats, so it is assumed that if saccharin causes any kind of cancer in humans, it is most likely to be this kind.) These figures are calculated for 50 million persons who have been steadily consuming saccharin in amounts equivalent to one 12-ounce can of diet soda each day of their lives. They may be compared with a current annual incidence of about 30,000 bladder cancer cases.

The risk might be higher than this if saccharin could also act by "promoting" the action of *other* carcinogenic agents to which people are exposed (such as smoking). There is, in fact, a small amount of evidence from animals and tissue-culture systems suggesting that saccharin at high dose can enhance the cancer-inducing potency of certain other chemicals. But even less is known about the mechanism(s) of "promotion" than of direct cancer induction—most importantly, how the effect might depend upon dose. If, for instance, enhancement resulted simply from the general debilitation that near-lethal doses of saccharin can produce, the effect should disappear entirely at nondebilitating doses. Given the paucity of our knowledge about promotion, its effect on human risk cannot now even be intelligently guessed.

Tests on Man

Let us turn from studies in animals to studies in man. Has there been an increase in bladder cancer rates that can be shown to be due to the increase in saccharin use that has occurred since World War II? There has not. However, this is not conclusive, because we probably could not detect a small effect (such as we would expect from the animal data), because other causes of bladder cancer have also increased in the period (smoking and occupational exposure to certain industrial chemicals together cause about 60 percent of currently diagnosed cases), and because not enough time may have elapsed for the latent period to have fully passed. Suppose, then, we look specifically among diabetics (who have been heavy users of saccharin since early in this century) for an elevated rate of bladder cancer. None has been found, but diabetics tend to smoke less than the rest of us (which might compensate for the cancer risk from their increased saccharin use), and also have elevated mortality risks from *other* causes than cancer and so might be dying first of these other things before the latent period for bladder cancer had passed.

A more sensitive procedure would be to query people with diagnosed bladder cancer in order to see if they had a history of excessive saccharin use when compared with a matched group of cancer-free persons. This is called a retrospective, or case-control, study. The two largest and most careful studies of this type on saccharin gave conflicting results: one completed recently in Baltimore on some 500 bladder cancer patients and a matched cancer-free group found no significant difference in saccharin use between the two groups, while the other,

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carried out in Canada, found *less* usage of saccharin among women with bladder cancer than among women without it, and a small *excess* of use in men with bladder cancer compared with men without it. All other retrospective studies were negative.

It is this single study in humans that, together with the rat results, supplies the evidential base for a saccharin ban. It is worth a look. The salient feature is that the difference in saccharin use among males was small: out of 480 men with cancer, 69 had "ever" used saccharin, while among the cancer-free group of 480 men, 43 had done so; thus, the difference consisted of only 26 men. The small size of this difference is significant. For unless the two groups are matched meticulously on all other factors that might be associated with saccharin use, we cannot securely rule out the possibility that so small a difference came about through association with some other dissimilarity between the two groups. There might be, for example, a chance, small excess of obese persons in the group with cancer, or a small excess in alcoholic consumption (diet sodas are often used for mixing cocktails), or a small increase in income (saccharin use increases with income and education); or there might be some other factor not yet identified. It is exceedingly difficult to match groups so perfectly as to eliminate all possible confounding factors. When the difference between the two groups in exposure to a suspected disease-causing agent is large, this problem can usually be ignored. (In this same Canadian study there was, for example, an enormous excess of heavy smokers in the group with cancer.) But when the difference is small and concerns only a small fraction of the matched samples, any conclusion suggested by it must be accepted with caution.

The wisdom of caution here is suggested by two additional facts. First, as mentioned, the effect among women in this same study was precisely opposite to the effect among men: there was *less* saccharin use among those with cancer than among those without it. (The actual numbers were 18 users of saccharin in a group of 152 women with cancer and 30 in the comparison group, also consisting of 152 women. This is a *larger* proportional difference than was seen in men, but it suggests the contrary conclusion.) It could be, of course, that a sex difference exists in humans as in rats. But it could also be that there are uncontrolled factors in the matching that produce false signals when we have such small numbers. And second, the equally good Baltimore study, which could have confirmed this difference in males, contradicted it instead.

Despite this disagreement, we can still draw a strong conclusion: the contribution of saccharin to bladder cancer rates in humans is,

. . . the contribution of saccharin to bladder cancer rates in humans is, if not zero, so small that it cannot be reliably distinguished from zero. . . .

if not zero, so small that it cannot be reliably distinguished from zero within the sensitivity of this type of study. That sensitivity is not overly high, but it is probably fair to say that if saccharin in its past patterns of use caused 10 percent or more of the 30,000 bladder cancer cases diagnosed each year (through initiation and promotion combined), it should have been securely seen in these studies. (Note that, because of the long latency between the exposure to a bladder carcinogen and the clinical appearance of cancer—typically twenty to forty years for the two potent agents we know about—the rates we now see reflect usage patterns of at least twenty years ago. Thus these results cannot assure us that no risk at all will become manifest in the future from increased saccharin use.)

How Sweet It Is

So much for the risks from saccharin. What are its benefits? It has minor uses as a flavoring agent in toothpastes and certain drugs, and it is believed by some to help reduce tooth decay. But its primary use is in diet control. Diabetics and their doctors, for example, view saccharin as a major aid in diet maintenance. It is not merely saccharin as a table-top sweetener that is valued here, but *specifically* the widespread marketing and easy availability of diet desserts, fruits, and drinks. These give variety to a diabetic's diet, permit him to travel widely without worrying about the availability of safe foods, and enable diabetic children to lead less

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dry and parsimonious lives than they would otherwise.

And saccharin is widely believed to be helpful in weight control. Some 22 percent of our population—more than 40 million people—are twenty-five pounds or more overweight. Some people may use saccharin products to lose weight, but a much larger number use it to avoid a weight gain that, all things being equal, would otherwise occur. Again, it is precisely the wide availability of foods containing saccharin that makes it not merely possible but also convenient to stick with a diet. And since obesity aggravates many diseases, a substantial health benefit may well result from having saccharin widely obtainable in varied forms.

These are the purported benefits of saccharin, but are they real, and how large are they? Unfortunately, there is a dearth of "scientific" evidence on these points. No one knows how many cavities might be prevented through consumption of saccharin-sweetened foods in place of sugared ones. No one has measured how much "quality" is added to the life of a diabetic by the ready accessibility of diabetic foods as compared with having only pills available. And no one knows how much weight would be either gained or not lost if saccharin (or some other artificial sweetener) were not available, nor how many more cases of heart disease, stroke, late-onset diabetes, and other weight-related illness would be diagnosed each year if foods containing saccharin were banned. We may note, however, that these benefits need not be very large to offset the risks of saccharin entirely: a few thousand heart attacks, strokes, and diabetic crises avoided per year among the tens of millions of saccharin users would do. That is a number so small that we could not exclude it by any conceivable study. It is, in short, as difficult to prove that small benefits do *not* exist as it is to prove that a small risk of cancer does.

Thus, in making the benefit/risk judgment on saccharin, the benefits must be assigned the value, not of zero, but of a wild card. The net effect that a saccharin ban would have on the public's health therefore cannot be known.

We do, however, have other forms of testimony about saccharin's benefits. Not only has Congress been flooded with letters—as *Science* magazine writes, "diet food fans by the millions have protested" the proposed ban—but we have as well the evidence of people's market actions *after* the saccharin risk was widely publicized. This is not insignificant, because consumers have first-hand knowledge (not always apparent to the "scientific" observer) of the value of diet foods to them, and their actions tell us that they find the benefits of saccharin worth the risk as this has been set forth to date.

Prohibition or Free Choice?

Given this situation, what would be an intelligent regulatory response? Two considerations greatly clarify this matter. First, this is *not* a situation similar to air pollution or to the contamination of the land with pesticides, where externalities prevent individuals from taking independent action to control their own fates, and hence require that a collective, unitary judgment on the overall risks and benefits be enforced. Instead, it is a *user-risk* situation, where the user is generally the only person exposed to danger and where he can choose whether to take the risk.

Second, there are great variations in the risk/benefit circumstances of individuals. We can, for instance, identify groups that may have elevated risks from saccharin: pregnant women, since their unborn children might be unusually sensitive (as the two-generation rat tests suggest), and children, who not only might be more sensitive but who also have such a long life expectancy before them that an induced cancer would have ample time to develop. We can as readily identify groups that are likely to have zero risk. All persons fifty-five years of age or older, for example, can probably use saccharin with impunity since the latent period for cancer induction would be longer than their remaining life expectancy. Also, adult women suffer no apparent risk to themselves: none of the epidemiological studies have found any risk to women, and none of the rat studies have shown significant numbers of tumors in females. Women and those over fifty-five, be it noted, comprise well over *half* the population! (The same kind of variation exists on the benefit side, too. There obviously are groups of people—the obese and the diabetic—who *already* have more than ordinary health hazards that can be reduced by saccharin and who hence can derive a more than ordinary benefit from it.)

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Any sensible regulatory effort must, then, take these wide variations in personal circumstances into account: what is needed is a variegated solution rather than a uniform one. This consideration should carry us far away from simple thoughts of banning all uses of saccharin-containing products, including good ones, and toward solutions that are aimed at specific groups with high relative risk or that rely on incentives to encourage the desired pattern of use. Consider these possibilities:

Any sensible regulatory effort must . . . take these wide variations in personal circumstances into account: what is needed is a variegated solution rather than a uniform one.

(1) Pregnancy is a temporary condition, so that temporary abstinence from saccharin use would eliminate all hazard to unborn children. This is a narrowly focused policy problem. Presumably, informing pregnant women, nursing mothers, and their doctors would largely solve it, as it does for other substances (such as certain drugs) that pose a danger to fetuses and infants.

(2) Childhood, too, is temporary. A prohibition on saccharin sales to minors (as we now prohibit alcohol), coupled with an educational program to convince parents of the hazard, would be one way to reduce this risk. Once again, this policy problem has a narrow scope and would not be efficiently addressed by a uniform ban on all uses of saccharin products.

(3) One solution relying upon incentives would be to put a tax on saccharin-sweetened products, thereby introducing an optionally large price difference between these and their sugared substitutes. This would discourage frivolous consumption of saccharin products, while still permitting persons with special needs for diet foods to obtain them.

(4) Finally, one could simply supply information about the risks and benefits of saccharin to consumers as the information becomes available, and let them make their own decisions.

Let us examine this last alternative in more detail. It envisions that people would evaluate their own risk/benefit situations and determine their saccharin use accordingly. Presumably, people with the greatest risk from other health problems would be primary users of saccharin. We *would* thus obtain a variegated solution that allowed for differences in individual circumstances and that also had the general form we want. Too, it would be *self*-adjusting, so there would be no administrative costs other than those involved in assembling and communicating the information needed for making intelligent judgments of net risk. (This information should, of course, include a description of bladder cancer symptoms, so that the chances of early detection among saccharin users could be improved. This cancer, like many others, is highly curable in its early stages.) And changes in the state of our knowledge could be rapidly accommodated; if, for instance, a great danger *were* ultimately proven, there is little doubt that consumers would cease using diet foods of their own accord. A simple program of providing information, then, has by itself many of the features of a desirable and workable solution, and it is already largely in place.

We might now ask what it is about saccharin that distinguishes it from other, greater risks we leave to individual choice. Why, for example, do we find ourselves serenely contemplating a person's plan to climb a dangerous Himalayan peak at the same time that we propose making it illegal for her to buy a can of Tab? The answer is simple: it is the 1958 Delaney amendment to the Food, Drug, and Cosmetic Act which, in its crucial phrases, runs as follows, "No additive shall be deemed to be safe if it is found to induce cancer when ingested by man or animal, or if it is found, after tests which are appropriate for the evaluation of the safety of food additives, to induce cancer in man or animal."

Why . . . do we find ourselves serenely contemplating a person's plan to climb a dangerous Himalayan peak at the same time that we propose making it illegal for her to buy a can of Tab?

Consider those words in light of the facts just reviewed. Several defects are apparent:

(1) The words presume a fine clarity in the

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The words [of the Delaney amendment] presume a fine clarity in the judgments of science that is not always there.

judgments of science that is not always there. There is no "proof," for instance, that cancer has ever been caused by saccharin when "ingested by man." Nor can anyone irrefragably assert that exposure of rat fetuses to near-toxic doses is "appropriate" for the evaluation of the safety of this additive. And is exposure through the umbilical cord what is meant by "ingestion"? Too, nowhere in this confident phrasing is there allowance for a situation that is very common when scientific techniques are stretched to their limit, namely, that equally well-performed experiments can give *conflicting* results. Five one-generation rat tests, for example, produced no tumors, while one did; and one major epidemiological study found a slight cancer risk in males, while all the others did not. Being able to repeat a result is, of course, the sine qua non for converting an isolated (and possibly aberrant) observation into a secure scientific fact, and in the absence of this replicability, there is no basis for making a decision.

(2) As has often been pointed out, the amendment takes a curiously one-sided view in ignoring offsetting gains: an additive would still have to be banned even if there *were* proven counterbalancing benefits!

(3) The words require that a *single* decision for the entire society be made even in the face of uncertainty concerning judgments of net risk. A more prudent course would permit people to make choices either way on an ambiguous issue so as to limit the damage from the wrong guess.

(4) The passage ignores the person-to-person *variations* in risk/benefit situations that any sensible public policy in a user-risk context would accommodate.

(5) Moreover, the Delaney amendment aims to solve another problem than the one at hand. It seems to presuppose a situation where businessmen (acting to maximize short-term profits and oblivious to the insidious long-term harm their products might cause) expose the public to needless risk. Yet the true situation here is that there is a *legitimate* disagreement in interpreting the information we have, and it is evidently the public's will rather than manufacturers' greed that the words of the amendment frustrate.

There is, then, a reasonable question whether this state of affairs truly is the intent of Congress rather than an unforeseen and unintended consequence.

Let us now sum up. Science cannot tell us how many potential human cancers swim in a can of diet soda, though it has made some guesses. What *can* be shown is that a weak cancer can be induced by saccharin in rats, but only under unusual conditions whose relevance to human risk is obscure. From epidemiology we learned that the number of human bladder cancer cases that might currently be caused by past patterns of saccharin use is certainly small, and perhaps zero. We know, on the other hand, that it is at least *plausible* that saccharin offers substantial health benefits to certain groups of people, that these benefits need not be large in order to offset saccharin's slight risk, and that, unless we know *for sure* that the benefits are imaginary, it would be a reckless gamble with the public's health to compel a ban on diet food products. We know that a simple program of informing the public would accomplish by itself most or all of the aims of wise policy. And we know that the impetus for a ban does not issue from a proven public injury but from a well-intentioned legalism whose full consequences probably were not foreseen. Finally, we know that the public has spoken against a ban not just patiently and politely, but with a mass roar.

... unless we know for sure that the benefits are imaginary, it would be a reckless gamble with the public's health to compel a ban on diet food products.

Indeed, the contradiction between what the public wants and what FDA officials think, in a somewhat Pharisaic exercise, they are obliged to do should give pause to those who wish to secure the public's true well-being. For behind this lies a profound question: *Is* the public always right, after all? This question, of course, concerns not only saccharin but the heart of democracy as well. ■

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Report of the President's Commission on Antitrust

Joe Sims

ANTITRUST has had bipartisan support since the Sherman Act became law in 1890. Both political parties have preached devotion to its principles, and most political candidates have promised vigorous action against the most notorious monopoly of their times. It used to be the oil trust, or the steel trust or the railroad barons, but today, it is the oil industry that is blamed for everything from high prices to shortages. Though both political parties claim the more active record of enforcement and though my own impression is that the Republicans should win that argument—if only because they have spent more time enforcing the antitrust laws and proportionately less time trying to rewrite them —I recognize that this is a barroom question which even statistical analysis will not resolve.

The issue is tremendously complicated by a lack of consensus, a schizophrenia, on what antitrust enforcement really is or should be. The near unanimity of opinion at the time the Sherman Act was passed did not last. Almost immediately, enforcement became a matter of great controversy, in part because the early targets of the act were labor unions and a number of labor leaders went to jail convicted of a criminal restraint of trade for their success in union organizing. In any case, within a mere quarter of a century (in 1914), Congress passed two additional comprehensive antitrust laws—the Clayton Act (which, among other things, exempted labor union activities from the antitrust law) and the Federal Trade Commission Act. The latter created an independent enforcement agency, the Federal Trade Commission, and expanded the notion of antitrust to include "unfair trade practices," thus giving legislative recognition to the idea that antitrust involved something more than economics.

As time passed, new concepts of mass merchandising took hold, putting increased competitive pressures on the traditional small retailer and eventually producing the Robinson-Patman Act amendments to the Clayton Act (1936). That Robinson-Patman is seriously described by some as an antitrust law shows how diverse are the troops that gather from time to time under the antitrust banner.

There were more additions to the stable of "antitrust" laws over the years. In 1950 came the Celler-Kefauver amendments to the anti-merger statute (Section 7 of the Clayton Act). These amendments made Section 7 into an effective tool for blocking anticompetitive mergers, one that has been aggressively used for this and other purposes by both public prosecutors and private plaintiffs. The decade of the 1970s has seen a tremendous amount of antitrust legislative activity: the repeal of the fair trade amendments to the Sherman Act (which had permitted states to allow manufacturers to control the retail prices at which their products were sold), the Antitrust Procedures and Penalties Act (which set up a regulatory system for antitrust consent decrees and changed Sherman Act criminal violations from misdemeanors to felonies), and finally, the Hart-Scott-Rodino Antitrust Improvements Act of 1976.

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Hart-Scott-Rodino was very controversial, so much so that an effort to kill it by filibuster was only narrowly defeated. Nevertheless, it was, by and large, sensible legislation. Certainly, the part of the act that increased the investigatory powers of the Justice Department's Antitrust Division was long overdue, and the notion underlying the second part, advance notification of significant mergers, is not radical in concept. The third part of the act, which allows state attorneys general to bring treble damage suits on behalf of injured consumers, is less clearly desirable, but even there, the strongest objections are practical ones. The notion that consumers should be reimbursed for damages actually caused by illegal conduct certainly is not in itself shocking.

However, Hart-Scott-Rodino is less important for its substantive content than for what it may portend for the near future. Along with other recent antitrust legislation, it may well signify a resurgence of antitrust fervor, still fed as in the past by populist fears of bigness and industrial concentration, but now also greatly assisted by the ravages of inflation. Antitrust is a perfect *political* answer to inflationary fears. There certainly can be no doubt that price-fixing contributes to inflation, and it is only a small step from there to the more general notions that the big corporations are the inflation villains and that the world would be better off with this political, social, and economic power broken into smaller units. While the equation is slightly different, much of the analysis is of the same approximate quality as that which justified the economic legislation of our last major crisis in economic confidence —the Great Depression—and there is obviously a risk that our legislative response to this crisis will be equally misguided.

Thus, there have been proposals like the late Senator Philip Hart's industrial reorganization bill, designed to facilitate the wholesale restructuring of specific "concentrated" industries. "No-fault" monopoly, as we will see, is being advanced as yet another way to get at the "problem," whatever the problem may be. Conglomerate merger legislative proposals of various kinds are surfacing, and much rhetoric is devoted to notions of "shared monopoly," undoubtedly on the premise that a more pejorative label will make it possible to challenge some industrial structures that are not otherwise reachable under the Sherman Act.

It is in the context of both the history of antitrust and the current intellectual activity that the recommendations of the National Commission to Review Antitrust Laws and Procedures (NCRALP) should be examined. NCRALP really dealt with three areas—regulatory reform, "big-case" antitrust litigation rules, and substantive proposals to change the antitrust laws. The last two of these are examined here. (For a discussion of the commission's regulatory reform recommendations, see "No Confidence in Old Trusts," pages 12–13, this issue.)

Background

The commission was proposed by Attorney General Griffin Bell, who hoped to find a way to deal with the obvious problem of big-case antitrust litigation. Bell inherited two giant cases —*United States* v. *IBM* and *United States* v. *AT&T*—and, from the beginning of his tenure, was interested in doing more than his predecessors to move both of them along. Early on, he suggested that perhaps big cases should be litigated not before a district judge but instead before Congress, and he still has not completely recovered from that idea. Yet, while his initial remedy may have been ill-conceived, he had a clear notion of the problem and NCRALP owes its existence to Bell's concern over *IBM* and *AT&T*.

The Antitrust Division did not greet Bell's proposal with wild enthusiasm. The division has continually opposed suggestions for an antitrust review commission, in part for bureaucratic reasons, but in larger part for fear that if the subject were ever opened for debate, more bad than good would result. (This concern is analogous to the fear of a constitutional convention, not for what it would be created to do, but for the unknown result it might produce.) After all, the Antitrust Division has never been a powerful agency. It has occasionally made a difference, but more often than not, when in conflict with another part of the executive branch, it has been the loser. In recent years, its record is much better, but this is largely post-Watergate, and is to some extent a direct reflection of the antagonism to presidential control that has characterized our national politics over the last five years. The much more usual outcome of a conflict between the divi-

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sion and another agency is that noted by Dean Acheson in his description of the oil cartel investigation in the early 1950s. After failing to get the Justice Department to stop what he viewed as activity inconsistent with U.S. foreign policy interests, Acheson appealed to what he called "our common superior." The investigation was stopped.

Certainly the division was not at all enthusiastic about tinkering with the Sherman Act, which is, after all, the "Magna Carta of free enterprise" and is generally perceived within the agency as a very successful tool for judicially adjusting the rules of the economic game to changing circumstances. Nor was there any desire to become embroiled in the continuing debate over monopoly, oligopoly, concentration, and efficiency, not to mention the "bigness is bad" arguments of antitrust populists.

Nonetheless, Judge Bell is a determined man, and it was soon clear that there would be an antitrust commission focusing on regulatory reform and "big case" litigation. The Antitrust Division was allowed to protect its flank by limiting the commission's mandate to working "within the framework of existing antitrust laws." As we shall see, this protection proved a trifle illusory.

"Big Case" Litigation Procedures

It is perhaps not surprising that a commission composed largely of people recommended by Judge Bell quickly agreed with him that there was, indeed, a big-case problem. What *is* slightly surprising is that, despite all the possible convenient villains—the complicated nature of the questions in litigation, the breadth of the substantive rules, the scope of the discovery process in modern litigation, the financial incentives for delay—the commission put the primary blame where it belongs, on weak judicial management. Throughout this portion of its report, the commission returns again and again to the notion that strong, effective, and continuing judicial control is *the* answer to protracted litigation.

The commission's litigation recommendations divide into two parts, those dealing with pretrial procedures and the trial itself and those dealing with the relief obtained after the litigation. Both are of substantial importance to antitrust lawyers but perhaps of less general interest to readers of this magazine. There are, however, several procedural suggestions that have substantive overtones or are likely to have major impact.

The commission directs attention to dilatory behavior by lawyers, leaving little doubt that in its view most of the blame falls on the defense bar. Although it recommends a number of neutral changes, it comes down hard on defense lawyers and their clients, recommending that defendants—when they lose—be required to pay interest on any damages awarded from the date the complaint was served rather than the date of judgment, thus adding a significant additional risk to litigation. This issue was the most divisive in the entire commission report: nine of the commission's twenty-two members dissented, including all but one of the practicing lawyers. In fact, except for Craig Spangenberg and Lawrence Sullivan, the only members voting in favor of prejudgment interest were government officials.

This change—if implemented—would obviously favor plaintiffs and increase pressures on defendants to settle rather than litigate. In effect, it would create a separate penalty for litigating if one lost, thus making a nuisance value settlement more attractive. No doubt it would discourage delay, but it would also encourage litigation blackmail.

The commission recommends another procedural change that would favor plaintiffs. The threat of private damage actions—in which antitrust plaintiffs can recover three times their actual damages—is considered by many to be more of a deterrent to collusive conduct than possible criminal penalties. In order to encourage private damage actions, the antitrust laws currently allow a *final* decision in a government action to be used as evidence of a violation in a subsequent private action. The prior government decision only establishes a rebuttable presumption of liability, however, and therefore is not considered very helpful by many plaintiffs' antitrust lawyers. The commission would assist private plaintiffs even more by amending the Clayton Act to ensure that ordinary collateral estoppel rules could be used in private antitrust damage actions. This would mean that, once the government proved a violation of the antitrust laws in court, the violation could not be rebutted in a subsequent private suit for treble damages. The commission recog-

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nizes that the "use of collateral estoppel may somewhat increase pressure on antitrust defendants to settle rather than litigate." In its view, the dangers of this effect were outweighed by the potential advantages in expediting litigation.

The chapter dealing with the relief that courts may award is an intellectual complaint about the real world. The commission complains—quite accurately—that relief has frequently been ineffective in antitrust cases, especially in cases dealing with industry structure, and assigns the blame to the courts' failure to fashion relief in a way that would most promote competition. The courts have, according to the commission, paid entirely too much attention to "private" interests—those of the defendant and its employees, customers, and suppliers—and too little attention to the "public" interest in competition. In addition, they have, inappropriately in the commission's view, too often attempted to balance these "private" and "public" interests in attempting to come up with a balanced relief proposal.

The commission sees two ways to solve the problem—preventing the consummation of more transactions pending the outcome of litigation (thus rendering relief unnecessary in more cases) and convincing judges to be more aggressive on relief issues, especially in monopolization cases. Thus the report endorses a much liberalized standard for the granting of preliminary injunctions in merger cases. It would grant a preliminary injunction where the plaintiff shows that he is likely to win; and even where that showing cannot be made, it would still grant the injunction where "significant, substantial and difficult issues of law" are raised and the "balance of hardship" falls on the plaintiff.

As Commissioner Gordon Spivack (former director of operations for the Antitrust Division) points out in his dissent, the anti-merger statute is forward-looking, requiring only a showing that the transaction "may" lessen competition. The "probability of success on the merits" standard thus requires, according to Spivack, only that the plaintiff demonstrate by "reliable probative evidence a reasonable probability of a reasonable probability of a substantial lessening of competition in a specific market." Where this meager showing cannot be made, Spivack argues that any restraint imposed on the transaction is just as unjustified as any other form of government substitution of bureaucratic judgment for the operation of free markets.

But when [the commission] examines antitrust enforcement, it seems to forget that this, too, is a form of government intervention—and the very wise test of regulatory necessity disappears.

Spivack has put his finger on an anomaly that can be explained only by the commission's prosecutorial bias. A comparison of NCRALP's work on regulatory reform with its work on antitrust enforcement reveals a clear dichotomy. In the regulated industry areas, the commission rails against unjustified government intervention and would require a showing of absolute necessity before any form of economic regulation is approved. But when it examines antitrust enforcement, it seems to forget that this, too, is a form of government intervention —and the very wise test of regulatory necessity disappears.

For example, the commission's preliminary injunction standard would be met in every anti-merger case brought by the government, unless one indulges the unreasonable assumption that the government would challenge a merger that was neither clearly bad nor even presented at least "significant, substantial and difficult issues of law." It is troubling to see that not only is there no careful weighing of the necessity for such a standard, but there is an outright rejection of the need for any such showing: "Private interests, *no matter how substantial*, are of reduced importance where there is a strong public need for preliminary relief that will preserve competition . . ." (emphasis added).

Although the report outlines the difficult mechanical problems that a small number of cases have presented, it makes no attempt to compare the costs of those cases with the costs of discouraging or preventing many mergers that show no sign of injuring competition. It is not a big step from an automatic injunction to a requirement for affirmative approval for mergers, as the various conglomerate merger proposals now being floated confirm. I am

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not sure where the balance lies, but the issue is surely important enough that it should at least have been discussed.

The report argues strongly that structural relief—that is, judicial restructuring of the offending industry—should be the preferred remedy for violations of Section 2 of the Sherman Act or Section 7 of the Clayton Act. In fact, the courts are sharply criticized for attempting merely to restore the status quo ante and for accepting partial divestitures, and it is concluded that courts should fashion whatever remedy is desirable to obtain "workable competition," including (where necessary) divestiture of more than the "offending" assets.

The commission asserts, with some justification, that it is often impossible to put things back the way they were before an unlawful acquisition (Section 7) or before the unlawful amassing of monopoly power (Section 2). It concludes that, given these difficulties, the public interest would be better served by an effort to affirmatively restructure the marketplace to maximize opportunities for competition. But here again, the commission's intellectual argument runs into the reality that courts will always be reluctant to impose their judgment of a proper market structure. Even where it is subsequently concluded that a particular acquisition violates Section 7, and especially where it is concluded that a market structure developed over many years violates Section 2, courts will be reluctant to intervene in the activist way urged by the commission. Shareholders, employees, and customers may well be only "private" interests—but the protection of "private" interests is the distinctive function of the judiciary, and it is unrealistic (and perhaps wrong) to expect a district court judge to suppress such concerns. The initiation of a Section 2 or Section 7 lawsuit does not transform a federal district court into the Federal Trade Commission or an industrial reorganization court; it is still a court of law, and its role is to adjudicate a particular issue between particular parties. While the case for wide-ranging structural relief has intellectual appeal, at least from a regulatory or law-enforcement perspective, it is not likely to influence the actions of many judges.

Perhaps in recognition of the great difficulties in this area, the commission urges the creation of a task force, composed of representatives of the Antitrust Division, the Federal Trade Commission, the Securities and Exchange Commission, the Internal Revenue Service, and the Federal Judicial Center, to develop a manual for divestiture. The manual would include information about various divestiture methods, examples of cases, various tools for measuring impact, analysis of the use of masters and other technical experts, various tax provisions, and other guidelines and suggestions for increasing the effectiveness of relief once a violation has been found.

Substantive Standards

The most controversial, and in many ways potentially most important, recommendations of the commission involve substantive changes in the antitrust laws. The report suggests amending Section 2 of the Sherman Act to broaden dramatically the "attempt to monopolize" offense, and it recommends congressional consideration of a "no-fault monopoly" statute aimed at "strengthening the ability of the Sherman Act to deal with persistent monopoly power." Enacting these recommendations (especially the latter) would greatly accelerate the transformation of antitrust enforcers from referees to regulators.

Attempt to Monopolize. The "attempt to monopolize" provision of the Sherman Act has traditionally been one of the least satisfactory from a prosecutor's perspective. At common law, a criminal attempt to commit a particular offense required sufficient actions to create a "dangerous probability" that the offense would be committed. Justice Holmes established the notion that this "dangerous probability" concept was included within the "attempt" provision of the Sherman Act, and over the years the courts have elevated that notion to a position of primacy among the relevant criteria.

No better example of the importance of the "dangerous probability" concept exists than the recent *Empire Gas* case, where the court of appeals found that the defendant had engaged in clearly anticompetitive activities (including threats, predatory price cuts, and misrepresentations) to prevent smaller competitors from competing, but found no violation because it did not believe that the defendant was close to achieving an actual monopoly. The Supreme

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Court refused to review the case, despite a strong plea by the Department of Justice that Supreme Court guidance in this area was essential. Certainly, therefore, this seemed a logical issue to put on the menu for a new antitrust commission.

The key problem here is really one of comparing costs and benefits. Although the notion of "dangerous probability" was abandoned long ago in the law of criminal attempts, it lives on in antitrust jurisprudence because of the fear that a more flexible standard would open the door to litigation designed to blunt or deter aggressive competitive behavior. One company's sale price may, to its competitor, be a predatory price cut, and an effort to expand market share is just as easily characterized as an attempt to exclude competition. Thus, the benefits of opening up the statutory standard for attempts must be balanced against the possible costs, and many knowledgeable observers —including the Antitrust Section of the American Bar Association and, historically, the Antitrust Division—have seen that balancing process as counseling against new legislation.

Happily, there is a possible middle ground but, unhappily, the commission's report dismisses it in a one sentence footnote.

Happily, there is a possible middle ground but, unhappily, the commission's report dismisses it in a one sentence footnote. The statutory standard could be loosened in government enforcement actions, but not in private litigation. Such a distinction would not be unique in the antitrust world, and indeed the "no-fault" monopoly notion pursued by the commission would, in all the forms presented, have been limited to government cases. This would give the government the necessary flexibility to deal with unilateral anticompetitive conduct, but would minimize the risk of chilling desirable aggressive competition. After all, the government can only initiate a small number of actions, and it would presumably give serious thought to the question of public injury before bringing any case. In any event, such a dangerous tool would not be available indiscriminately to any disgruntled competitor.

This middle ground has historically been favored by the Antitrust Division and was recommended to the commission both by the executive order establishing it and by Donald I. Baker, the former head of the Antitrust Division. Amazingly, it is not even analyzed in the commission's report. Instead, the report recommends changing Section 2 of the Sherman Act to require a finding of an attempt to monopolize when, after weighing the defendant's intent, its present or probable market power, and the anticompetitive potential of the conduct in question, a court determines that the conduct "significantly threatens competition" in a relevant market.

The commission also recommends a second addition to the Sherman Act to prevent the use of the Areeda-Turner test for predatory pricing. Professors Philip Areeda and Donald Turner have popularized the notion first advanced in their 1975 *Harvard Law Review* article that, as a matter of law, any price above marginal cost (or, as a more accessible proxy, average variable cost) should be presumptively legal, since marginal-cost pricing is economically efficient and thus desirable. The Areeda-Turner test has, in some courts, been slightly recast to read that any price at or above marginal cost by definition cannot be predatory. This revised test has gained wide acceptance in the courts, in large part because it is easily administrable. Not coincidentally, it provides, as does the "dangerous probability" standard, an easy means for summary disposition of litigation seen as mere competitive complaining.

Like the per se rule against price-fixing, this test may conceivably produce a wrong result from time to time, but one can be reasonably sure that the costs of searching out the rare exception far outweigh the benefits of finding it. In the vast majority of cases, marginal-cost pricing should be encouraged, not challenged. Unfortunately, the commission was apparently determined to take care of those rare circumstances when a "dominant" firm—a term never defined in the report—uses its superior efficiency "unfairly" to disadvantage some struggling new entrant.

Of course, one could agree (as Areeda and Turner would) with the abstract proposition that, in some circumstances, pricing above marginal cost could be predatory, and still

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have serious qualms about changing the language of Section 2 of the Sherman Act. At the least, a recognition of the trade-offs involved in such a decision—and an analysis of them—is necessary. And certainly, the alternative of turning only the government loose, rather than allowing any disgruntled competitor to rush into court, deserved discussion in the commission's report. Instead, the report recommends what would be the first substantive change in the eighty-eight-year-old Sherman Act without any analysis of these crucial issues.

In so doing, I should note, the commission was actually moderating its original view. In December, it voted twelve to zero to recommend a "unilateral restraint of trade" statute. Led by Commissioner Maxwell Blecher, the commission was seeking a remedy for every wrong, or as Areeda and Turner put it, seeking "to use [the attempt clause] as a tool to control distasteful business behavior." The statute included in Blecher's separate views is an example of what was under consideration; it would prohibit *any* conduct engaged in "with the specific intent to restrain trade." In the vast majority of cases, where the conduct is ambiguous and there is no direct evidence of intent, this issue of liability would have to go to a jury.

Where Blecher and his supporters saw no great danger, I see the potential for disaster. Such a statute would be roughly equivalent to opening up the Federal Trade Commission Act (prohibiting "unfair methods of competition") to private enforcement. The probability that every unsuccessful competitor could demand a jury verdict on whether a price cut was undertaken with the "intent to restrain trade" or was merely hard competition would certainly discourage aggressive competitive behavior. Blecher accepted that possibility, but believed that it was more important that anyone injured be enabled to recover his damages.

Given this state of affairs, perhaps one should be happy the commission ended up where it did. It took hard work by its staff, Chairman John Shenefield (the current head of the Antitrust Division), and Senator Edward Kennedy to beat off the Blecher proposal, and it may well be that the final recommendation is the best that could have been achieved under the circumstances. Still, the report must stand on its own merits, intra-commission politics notwithstanding, and when evaluated on that basis, this careless approach is disappointing and ultimately unpersuasive.

No-Fault Monopoly. As noted earlier, the Antitrust Division had no desire to get involved in rewriting the antitrust laws, fearing unattractive and perhaps irrational results. But that fear was not shared by all the parties involved, particularly the FTC. The FTC decided to use the commission to make some progress on what it saw as important antitrust initiatives. Professor John Flynn of the University of Utah was recruited as a consultant and the "no-fault" monopoly effort was under way.

Flynn's original testimony was very hardline. Despite the language of the executive order restricting the commission's work to the "framework of existing antitrust laws," he argued, "no-fault monopoly" was clearly within the mandate because it was part of the solution to the "big-case" problem. It would shorten the trial itself, and that is the most direct way to deal with protracted cases. Although this rationale was shown to be probably erroneous and was later abandoned, Flynn, in his testimony, placed most of the blame for protraction —and for what he viewed as inadequate remedies in monopolization cases—on the need to prove "bad" conduct. In Flynn's view, the key issue in a monopolization case should be monopoly power, since that was the evil, no matter how the power was created or maintained. In other words, even monopoly power that results from superior efficiency must be destroyed. Thus, his "no-fault" monopoly proposal: once the government proved the existence of monopoly power, the defendant's liability would be established and the case would immediately move to the remedy stage. The remedy would be dissolution, unless the defendant could establish that dissolution would result in the loss of substantial economies of scale (not including managerial or financial efficiencies).

The commission immediately perceived that it was up to its ears in the "Great Concentration Debate." If there were any doubts left, they were destroyed by the testimony of Areeda, whose *Antitrust Law* (written with Turner) was cited as the intellectual base for Flynn's proposal and by the subsequent debate between former Solicitor General Robert Bork, now at the Yale Law School, and Michigan State University economist Walter Adams.

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Areeda defended the intellectual concept, but carefully withheld any definitive opinion on the practical workability of legislation based on it or even the possibility of drafting such legislation. He cautiously agreed that the commission should consider the concept while clearly separating himself from Flynn's testimony, especially on the relevance of managerial and other non-scale efficiencies. In addition, he recognized the potential costs of this form of government intervention, and thus he argued that the persistence of monopoly power over a substantial period of time (at least five and perhaps ten years) was a critical prerequisite to any enforcement action. All in all, Areeda could be viewed as only a lukewarm supporter of a legislative proposal.

Bork and Adams turned out to provide the best entertainment of the commission hearings. Bork blasted the basic "no-fault" concept, arguing convincingly that eliminating the "bad conduct" element of a Section 2 trial would be a flawless prescription for purchasing shortness of trials at the price of rational outcomes. To Bork, persistent monopoly power (if it ever really existed, which he doubted) was much more likely the result of efficiency and better performance than predatory conduct. Thus, simply to assume the existence of predatory conduct would be wrong and, therefore, to dispense with the conduct requirement would reduce consumer welfare, since the most efficient competitor would be subject to attack and dismemberment because of its very efficiency.

Adams bemoaned the failure of government antitrust enforcement, which had resulted, in his view, in rampant monopoly throughout the economy. Although he thought the "no-fault" approach was inadequate, it was a step in the right direction—the ultimate goal being, his testimony would suggest, a rule forbidding any company from employing over ten people, thus making the economy very competitive indeed with everyone except the rest of the world.

After all this, the commission was sharply divided, with some of its members favoring endorsement of a "no-fault" proposal, some fiercely opposed, and some arguing that the present state of the law was fine so long as judges read it the way they did. The FTC submitted a modified recommendation limiting Flynn's proposal in various ways, but eventually the commission chose merely to recommend congressional study. Clearly Chairman Shenefield and the commission's staff were quite skeptical about the "no-fault" concept, and their skepticism was a major factor in the FTC's failure to carry the day completely.

... in this respect, the report is yet another step in the transition of antitrust from negative second-guessing and post facto punishment ... to affirmative regulatory intervention.

Still, one has to concede that the FTC won a victory. It certainly raised the visibility of the "no-fault"' notion, which was originally introduced by Senator Philip Hart in 1976 but quickly faded into obscurity. And it got some generally favorable quotable language from a presidential commission. The commission chose its words carefully, of course, but details and caveats tend to be washed away by the tides of time. Thus, in this respect, the report is yet another step in the transition of antitrust from negative second-guessing and post facto punishment—the law as referee—to affirmative regulatory intervention.

Conclusion

Obviously, Senator Kennedy's ascension to the chairmanship of the Senate Judiciary Committee has enormous potential significance for the future of antitrust legislation. It becomes even more significant when combined with the fact that both the Antitrust Division and the FTC are headed by very aggressive people—albeit with some significant differences in philosophy and approach—and with the presence in the White House of a President who has positioned himself as an independent populist. When we add to that the fact that a presidential election is less than two years away and that inflation will probably persist until then, we have all the ingredients for a new surge of antitrust activism. The NCRALP report is, in this context, a reformer's document, and the true test of its impact will be its capacity to generate new legislation in the coming two years. ■

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REFLECTIONS ON THE ELECTION COMMISSION

An Interview with Neil O. Staebler

Conducted by Nathan J. Muller

Neil O. Staebler was one of the original six members of the Federal Election Commission (FEC). A former chairman of the Michigan State Democratic Central Committee (1950–61), member of Congress (1963–65), and unsuccessful gubernatorial candidate (1964), Staebler was named to the FEC in large part because of his service on President Kennedy's 1961 Commission on Campaign Financing and on the Twentieth Century Fund's 1970 Task Force on Financing Congressional Campaigns. While on the commission, he earned the disapproval of the labor movement for casting the deciding vote in favor of the Sun Oil Company's political action committee in a controversial FEC opinion, a vote that probably cost him any chance of being reappointed to a second term when his first expired in 1977. The naming of his successor, Democrat John W. McGarry, sparked a legal challenge by Staebler and Common Cause, but the challenge became moot when the Senate confirmed McGarry and Republican Max Friedersdorf on February 21, 1979.

Staebler discusses the appointment controversy, FEC regulation of election campaigns, and Congress's relation with the commission in the following edited transcript of an interview he gave to Nathan J. Muller, editor of the Washington newsletter, Political Action Report. *The interview raises a number of points that relate directly to an article by* Buckley *v.* Valeo *attorney John R. Bolton and a response by former FEC general counsel John G. Murphy, Jr., both carried in REGULATION last year (volume 2, numbers 4 and 5).*

The FEC and Congress

Q: From the start, the Federal Election Commission has been criticized for being a "captive province" of the Congress? Is it?

A: Inevitably members of Congress are closer to the election process than other candidates. They follow developments in election law more closely and they are here in Washington, so they tend to get better than average service from the commission. But the commission has been conscious of the problems of nonincumbents and has always tried to be evenhanded. I think it has succeeded. Nevertheless, there are many aspects of incumbency that affect the process, among them the fact that members of Congress set the commission's budget and have the opportunity to review its proposed regulations and veto them.

Q: Has not the FEC been reluctant to deal with matters affecting incumbents?

A: No. Just the reverse. The FEC consciously braces itself against the danger that it might seem to favor incumbents. The legislative veto plays a role in what the commission does in that the commissioners may not try to do things that have been vetoed before. Take, for instance, our efforts to get a simpler way of having committees and candidates file their reports. We were rebuffed in this, one time officially and several more times unoffi-

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cially. So the candidates and committees for Senate races still file with the secretary of the Senate and those for House races with the clerk of the House; then the reports are transferred to the FEC. There are other instances where we had difficulty selling a program to Congress. But as for doing things for incumbents or against them or neglecting challengers, no.

Q: In your years on the commission, did you detect any urge on the part of Congress to protect itself?
A: Yes, especially through the legislative veto. There was a serious problem several years ago when Wayne Hays was chairman of the House Administration Committee, which has oversight over the FEC. We had a running battle with him for about a year. During that time he tried to influence the commission in a number of different ways. He was against the act to begin with, and then after it was passed he tried to influence us to the extent of actually trying to change specific regulations. We strenuously resisted. We told him that if Congress wanted to veto something we had done, it could, but that an individual committee or individual member did not have veto power. Apart from that, we never had a serious effort by a member of Congress to change any FEC decision. Most congressmen, an overwhelming number, took us as a necessary evil—or even a desirable influence—and did not attempt to tamper.

Q: Is this still a potential danger?
A: There's always a potential danger. Part of it arises from the fact that there's always a borderline or hazy area in regulations. If I were in Congress, I would be averse to giving a commission like the FEC carte blanche to do anything it wanted. The commission is a small body and its members cannot know everything: it could conceivably go off on a tangent. There needs to be a way of holding the whole process to some kind of accountability.

I would be averse to giving a commission like the FEC carte blanche. . . . There needs to be . . . some kind of accountability.

Q: But should Congress be able to veto the regulations of the agency designed to safeguard the integrity of the federal election process?
A: There has to be some sort of control, some final accountability. I think the legislative veto, the way it is set up, is a pretty good method of providing that. The FEC would like, however, to shorten the present veto process. As things stand now, proposed regulations have to lay before each house of the Congress for thirty legislative days. That, in effect, is ninety calendar days, and, on occasion, we found that this delayed the adoption of regulations by nearly a year. The FEC is urging Congress to shorten the waiting period to fifteen legislative days, which ought to allow reasonable opportunity for review.

Q: Are incumbents and their campaign committees given priority in terms of auditing or investigating questionable campaign practices?
A: No. In fact, the random auditing program the commission uses, a program that is subject to considerable attack by Congress, covers all the campaigns for a given seat and all are handled together —incumbents, as well as major and minor party challengers. Results are announced simultaneously, unless some serious violation is encountered that holds one contest up for a longer period of time. There is a modest threshold for the number of dollars spent, so some of the tiny campaigns are exempt from auditing. But minor candidates that spend over the threshold are handled with the rest. Incumbents are not given any priority in either starting or delaying audits.

Legal Complexifier?

Q: Since its creation, the FEC has had nine different individuals as members. Five have been members of Congress, two (including one of those five) have had state party experience, one was associate general counsel to the AFL-CIO, and the two newest members, John McGarry and Max Friedersdorf, have strong ties to members of Congress and the political party hierarchies. Do you believe the cumulative result of those backgrounds is an agency prone to complicate an already complex law?
A: It is not the fact that many have been members of Congress that produces complication in the law. The complexities arise partly from the circumstances of politics and partly from the inclination of lawyers to make things neat. Politics is hellishly complicated. After thirty years in politics, I thought I had seen most of the kinds of situations that could arise. I could not have been more wrong. From the time I came on the commission, there wasn't a week when three or four new things I'd never even heard of before were not brought before us. Americans are an inventive people, living in a highly pluralistic society; and Congress, when it wrote the law, didn't envision the true de-

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gree of their inventiveness. When the commission writes the regulations, it is in somewhat the same boat. Moreover, nobody—nobody, I repeat—knows enough about the political process to write flawless laws. Lawmaking is always a process of blundering in, trying to avoid major errors, but still getting only an approximate coverage of a particular situation, and having to find out what is wrong after the measure goes into effect. Over a period of years, one hopes to reduce initial error and learn to correct it more quickly. But still, because of our pluralism, politics is a very complicated field.

Now the other factor that enters in here is that lawyers are bound by their training to generalize and to produce something that is manifestly fair and defensible on legal grounds from every point of view. They consequently try to take into account all the possible exceptions and the deviations. This makes for a law that is very complicated when you try to apply it. The Federal Election Campaign Act *is* complicated, but it is to the credit of the first commission that the act is a whale of a lot less complicated than it would have been had that commission not forced the attorneys to realize that not everything can be regulated.

A good illustration of the problem is the battle that took place over the allocation of party expenses arising from operation of candidate and party headquarters. It seemed to the attorneys that campaign headquarters' expenses were contributions to candidates and therefore ought to have been charged to candidates, especially since the issue came up when we were in the period of candidate ceilings. The majority of the commission agreed, but at the same time believed it would have been impractical to require the allocation of those expenses. That would only have imposed a mountain of bookkeeping on parties and candidates. How, we asked, could the general principles of the act possibly be compromised if we ruled that joint campaign headquarters were an expenditure by the party and not attributable to candidates? After all, if one tries to apply the same principles to both parties in the same ways, one is not likely to play favorites or upset the balance. So we won that argument and got a much simpler arrangement—namely, expenses incurred by the party for benefit of all candidates are not contributions to any particular candidate.

Q: Some critics accuse the FEC of tampering unnecessarily with the regulations and attribute this to lawyers and others who have no concept of how their meddling affects campaigns. What role have attorneys and other staff members played in the decision-making process?

A: The tampering should not be attributed to attorneys, since it is the business of attorneys to be as literal as possible. The tampering is done by the commission when it tries to relax a point in the law. But that is what I consider to be the chief role of the commission—trying to be practical in applying the act. "Tampering" is how the commission can get the attorneys to back away from their hard and fast literal interpretations.

No one can write laws that cover every circumstance. So, in applying a law, there is always the need to decide about its intent—to look up the legislative history, other prior laws, and any illuminating judicial decisions and, after doing that, to make a judgment. Then, the question I've always asked is: "Can I stretch the provision in question far enough in the direction of practicality, or should it be rewritten as a new law?"

If the results are very bad, the commission will throw the ball over to Congress and recommend changes. Six commissioners are correctives against each other as to what the purpose of the act is, for none of them thinks alike.

Other Perspectives Needed?

Q: Would the commission benefit from the perspectives of minor party leaders, state and local election officials, professional auditors, or even educators?

A: The commission benefits from all the perspectives it can get. The question is the price to be paid for one of those perspectives. It would not be advisable to have a narrow perspective because the commission is so small that one uninformed vote hurts very much. The thing most lacking on the commission is party experience. Most congressmen do not in fact have much party experience and really do not know how the parties operate. The greatest potential hazard the FEC presents is the damage it might do to the political parties. Joan Aikens and I were the only commission members who have really had any party experience. We struggled hard and managed to avoid a lot of damage, but this area remains a hazardous one. Ignorance of party functions is characteristically present in those from an academic or a third-party background. It is important that future appointments take into consideration the breadth of an individual's experience.

Q: But wouldn't most candidates say they have no need for political parties—or, at least, isn't that how many of them act?

A: Congressmen have always felt a little separate from their parties and have not wanted to trust

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any organization other than their own. Senators are more inclined to trust the party because it is so hard to set up an adequate statewide organization of one's own. I believe the congressman's mistrust for parties is one of our greatest political shortcomings in the recent past and one of the greatest hazards for the future. A political system without parties would be chaos. Parties serve the purpose of bringing people together, of working out compromises on those issues the people have the tendency to get all wrought up about, of educating voters to a broader appreciation of political problems. One can visualize greatly weakened parties with a national primary or with the primary system made universal not only for the presidency but in every state. There would then be very little candidate recruitment, candidate training, and the development of experience—only chaos.

Small Campaigns

Q: Critics of the FEC charge that the agency is more attuned to the sensitivities of Congress than to the financial and recordkeeping problems present in many campaigns. Is this true?
A: We had a study made by Peter Hart and Richard Wirthlin two years ago. They found that the campaigns most likely to have trouble with the forms were the very tiny ones—those of the minor-party or vanity candidates—where there was not much manpower available and where the candidate, the candidate's wife, and a few friends tried to do everything. The larger organizations, no—they did not find the necessary recordkeeping difficult. I think the task will become increasingly easy as candidates get more used to it. Also, the commission is recommending amendments to the campaign act that would cut down filing by more than 50 percent.

Q: Why does the commission bother to cajole the non-filing minor-party candidates or unsuccessful vanity candidates into compliance?
A: The reason is that once the FEC accepts noncompliance for those whose spending is above the threshold, the seriousness of compliance is eroded. Candidate noncompliance was above 20 percent for 1977, the latest year for which a compilation has been made, and this suggests that important candidates could fall into the habit of noncompliance. The commission starts at the early stage with non-filers. It notifies everybody, and does it at a time when voters are likely to be paying attention to the matter. After the election, it sorts out those who did not get many votes or spend much money, and does not go any further with them.

Is Regulation Stultifying?

Q: Has the stable regulatory framework created by the act restricted campaign activity to the extent of discouraging more qualified individuals from seeking office?
A: The Hart-Wirthlin study shed some light on that matter. They asked the question another way: "What were the factors that entered into your deciding to run or not to run?" Ability to raise money was first on the list, and regulatory problems came in fifth or sixth—only a fraction even mentioned them. No one said he or she was deterred from running by the fact of regulation.

I believe that, over time, the expectation that the process is honest will encourage people to run. Electoral politics used to be such a murky process. If the other guy was going to get away with all sorts of shenanigans, and if the candidate didn't want to indulge in them himself or thought he couldn't, there would be an inclination to say, "let's get out of this mess and let somebody else do it."

Q: Has the act reduced the spontaneity of the average citizen's participation in election activities?
A: Most citizens are not aware of the act, except perhaps for the knowledge that they cannot give more than $1,000 to a candidate in either the primary or the general election. Since not many people give $1,000, the limit is not much of an inhibition. I have found that those who used to give more than $1,000 are in a way glad, and I have not found any great "chilling effect" on individuals.

Labor Cases

Q: In recent cases involving the AFL-CIO, the Public Service Research Council, the National Right-to-Work Committee, and the National Education Association, the initial penalties were very different and yet the amounts involved in the infractions were pretty much the same. Why?
A: Let me explain by telling the story of the AFL-CIO case. Actually I didn't think there should have been any penalty at all in that case. It involved the AFL-CIO political action fund (COPE), which followed the practice of collecting money during the two-year period before the elections—when, of course, it had no use for the money. So the fund would loan the money to the AFL-CIO's education fund and when the election came around, the education fund would repay it at 6 percent interest. The commission followed the law's prohibition against commingling of funds (commingling frequently results in hanky-panky). I maintained that

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this was not a case of commingling—or that it was a case only in the most semantically strained way. The education fund knew the money was borrowed, could have borrowed the money from a bank, but chose to borrow it from the political action fund. What the latter got back was not tainted money, but its own money. The commission, however, believed so strongly that commingling ought to be prevented and was so damn literal on the matter that even Commissioner Harris, the AFL-CIO's former attorney, thought the union was guilty.

The FEC's first conciliation proposal, which I voted against, was that the education fund forfeit the $300,000 it had borrowed and pay a $10,000 penalty. The AFL-CIO took us to court, refusing to settle. The judge said no on the $300,000 and yes on the $10,000 fine, whereupon the AFL-CIO appealed. The case is still in the courts.

Q: Can the AFL-CIO continue the practice in the future if the $10,000 fine is rescinded upon appeal?
A: No. It agreed in the conciliation agreement it would not do that in the future.

Another kind of commingling that the commission has to work hard against involves the funds of state party committees. It is, of course, illegal for *federal* candidates to take contributions from corporations but, in many states, it is not illegal for *state* candidates to take such contributions. So there is a problem if a party committee commingles corporate and noncorporate contributions and then makes a contribution to a federal candidate. We urge those committees to set up two funds, one for each kind of contribution.

Q: How do you explain the FEC's reluctance to rule on the reverse checkoff method of collecting contributions used by the National Education Association (NEA)?
A: There was no reluctance to rule—in fact we reached a decision very rapidly. But NEA put up so many defenses against it, and the question came back so many times during the early part of the conciliation process, that the commission wound up considering four or five different proposals. Another thing the NEA tried to do (and this was one more reason for the delay) was to get our ruling overturned in Congress by lobbying the House Administration Committee to attach an amendment to the FEC authorization bill to permit the reverse checkoff.

Q: How successful was this attempt?
A: It did not carry in the House Administration Committee. Finally, after all the legal maneuvers were exhausted, the case was settled in court, in the commission's favor. The FEC could not have moved any faster than it did.

Q: Did you detect any pro-union bias at all in your years with the commission?
A: Well, Tom Harris has been very careful, though I think I see some pro-union thinking he cannot well avoid. And I see it in myself, which is not surprising. Almost any Democrat, of course, has an inclination to regard unions as more beneficent than business. But I think I bring a fairly balanced approach to the commission because, though all my life in Michigan I worked with unions, I tried to keep the Democratic party from becoming a labor party—and did so with great success. Of course, even the top labor people recognized that it would not be desirable to let that happen.

I was accused of being anti-union in our decision on Sun Oil Company's Political Action Committee (SUN-PAC) in 1975. That decision, however, was not anti-union. I am a strong believer in everyone's being able to participate in the political process, and I think the law required the decision I reached. People accused me of stretching the law. I did not, but if I had had to stretch, I would have, because I think it would be very bad government, very bad politics, to permit one part of our society to do things forbidden to other parts.

Q: The people at the National Right-to-Work Committee (NRTW) have charged that the FEC is organized labor's newest weapon. They claim that when they asked for an advisory opinion on their plans for organizing a political action committee (PAC), Tom Harris deliberately stalled in answering—and then the staff's draft opinion approving operations of NRTW's PAC was suddenly withdrawn just before the commission was to rule on it. What has accounted for the long wait since NRTW's initial request in January 1976?
A: Certainly not Tom Harris or the withdrawal of the draft opinion. Two other things were involved. First, the request was ambiguous on the subject of membership and considerable time was consumed in getting NRTW to spell out what it meant by members. Second, while this was going on, there was a complaint (which automatically moved the matter to a different procedural track) on the subject of membership organizations whose members had no discernible authority or privileges of membership and whose only relationship to the organization was that of contributor.

As it turned out, National Right-to-Work was violating the important principle on which that

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complaint was based—a principle that has arisen in a number of other cases. The law says membership organizations may form PACs and solicit their members. But NRTW is not a membership organization—in fact, article 7 of its by-laws even says it has no members. What it was doing was to use membership as a come-on. It was soliciting contributions for National Right-to-Work activities and calling the contributors "members." We told the officials at NRTW they ought to revise their by-laws so that membership provided some rights, gave members some control, however tenuous, over the organization. We told them to do it right, and eventually we filed suit.

Q: So it is only the membership question that caused the delay and the suit?
A: Yes. And, incidentally, the right-to-work people were not the only ones to have trouble with this membership question: other outfits were held up too. By the way, the case is in discovery now and is set for trial on July 9.

The Appointment Process

Q: When you wanted to be reappointed to a second term, didn't you ask Leonard Woodcock to intercede for you with the Carter administration?
A: Yes, I did. But Leonard did not want to get involved and referred me to Woody Ginsberg at the United Auto Workers. I could see that Ginsberg also didn't want to be involved so I let the matter drop. I wanted to give Woodcock a clear idea why I had acted as I did in the SUN-PAC decision. I thought he was prejudiced, and it was being said that there was a strong union objection to me. I wanted to serve, not a full term, but two years more—through the 1978 elections—in order to help correct some shortcomings we had uncovered in the act. But I found that getting union support was impossible.

Q: What do you think of the way President Carter handled the two recent FEC appointments?
A: His treatment certainly carried the implication that he was standing at something less than arms-length from the FEC. First he appointed—or, rather, tried to appoint—John McGarry for the Democratic seat and Richard Zagoria for the Republican seat. The Republicans objected to Zagoria, not because he was not a splendid person, but because he did not reflect a Republican viewpoint (they thought he was too liberal) and because he was first approached—to see if he would serve—by a Democratic member of the commission. That suggested to them that he would not be a wholly independent commissioner.

Q: Was it proper for a Democratic member of the commission to try to line up a candidate for a Republican seat, particularly in view of the understanding that the President would appoint from a list drawn up by the Republican congressional leadership?
A: It looked bad, but I don't think it was. Members are constantly trying to suggest good people.

... the conclusion is inescapable that McGarry's appointment was ... an attempt by O'Neill to keep a thumb on the FEC.

Q: Do you have anything to say about the way in which your successor, McGarry, was chosen?
A: The FEC Act provides that "a member of the commission may serve after the expiration of his term until his successor has taken office" and it provides that members take office after being appointed with the advice and consent of the Senate. Now McGarry was not confirmed by the Senate. Common Cause and I maintained—in a suit in the U.S. District Court of the District of Columbia—that there was no vacancy until my successor was confirmed, so McGarry could not receive an interim appointment to fill a vacancy. The President was treating this appointment like any other kind of administrative appointment—as though the act itself had no significance. We lost the case in district court, Common Cause appealed, but since McGarry has now been confirmed, the government will almost certainly move to dismiss the case as moot.

Between McGarry's appointment and the district court's decision, I did not vote on commission matters or draw a salary. And, of course, even if my case had been won, all the President would have had to do would have been to name somebody whom the Senate would confirm. And certainly the senators would have confirmed any one of dozens of people in my stead.

Q: Common Cause has called McGarry's interim appointment "shabby politics" and has implied that it smacked of a "political payoff" to House Speaker Tip O'Neill. Is Common Cause close to the mark?
A: I think the conclusion is inescapable that McGarry's appointment was in some way an attempt by O'Neill to keep a thumb on the FEC. ■

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Preference, Prejudice, and Difference—
RACIAL REASONING IN UNFREE MARKETS

Walter E. Williams

THE MOST STRIKING FEATURE of U.S. racial relations today is how much we spend to regulate the expression of various kinds of racial reasoning in our behavior. The purpose of this spending is to promote racial justice. But in no small measure, the conspicuous social programs we have brought into being in the attempt to realize this purpose have themselves contributed to racial strife and mistrust, while doing little to ease the problems of racial inequality. Why?

There is general agreement that minorities, at least in the past, have suffered injustices at the hands of the majority. But agreement is not as readily reached on what the remedies should be. Much of the difficulty stems from the fact that racial problems are discussed mostly in moral terms and in value-laden language. Since there is no thoroughly accepted standard for testing moral statements, there is not always a rational way to settle these arguments. Another part of the difficulty stems from the imprecise and ambiguous use of language by scholars and laymen alike. In analytical usage, it is necessary not only to separate the connotative from the denotative (literal) content of words, but also to make precise and operationally useful distinctions. My modest aim here is to suggest more precise ways of analyzing racial problems and to show how these ways will help us to understand the problems better and hence promote more effective policy.

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Working Definitions

The three words I am seeking to demystify—to restore to their strict (denotative) meanings—are discrimination, preference, and prejudice. I will also consider briefly the matter of real differences.

Racial Discrimination. Discrimination—as distinct from those things that produce it (preferences, prejudice, and real differences)—may be defined as an act of choice based upon utility maximization, and racial discrimination as an act of choice wherein racial attributes provide the criteria for choice. In this view, racial discrimination does not differ in any fundamental sense from other kinds of discrimination. All selection necessarily and simultaneously requires nonselection—that is, choice requires discrimination. When we preface the word "discrimination" with the word "racial," all we do is to state the attributes selected as the criteria of choice.

Our lives are largely spent discriminating for and against selected activities, objects, and people. For example, many of us discriminate against those who have criminal records, who bathe infrequently, and who use vulgar speech. Some employers discriminate against applicants who speak with a foreign accent, or have low intelligence, or cannot read, or went to the "wrong" college. There is also evidence of discrimination in politics—not many short men have been elected to the U.S. presidency. Furthermore, personal discrimination is not

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consistent. Sometimes people discriminate against theatre in favor of parties, against women in favor of men; and at other times the *same* people do the reverse.

When a choice is made on the basis of race, that choice *may* reflect the preferences of the chooser for a particular race, but it also *may not*. It is impossible for an observer to say whether choices based on a particular physical feature reflect the indulgence of preference (tastes) *or* the attempt to minimize information costs (prejudice) *or* the recognition of real differences. Let me spend some time on the distinction among the three.

Racial Preference. In everyday language as well as in economic analysis, an individual is said to prefer A to B if he places a higher value on A than on B. In economic theory we postulate that each individual has a consistent set of preferences—that is, tastes—and chooses the combination he most prefers from the available alternatives. When we are speaking as economists, there are no objective criteria by which we can judge whether one set of preferences is "better" than another. We cannot prove, for example, whether it is better or more righteous for a person to prefer the wines of Bordeaux to those of Burgundy or to prefer blue cars to red cars. The most we can ever objectively say is that, *given his preference pattern and income and price constraints*, the chooser is—or is not—doing the best he can.

It is impossible for an observer to say whether choices based on a particular physical feature reflect the indulgence of preference (tastes) or the attempt to minimize information costs (prejudice) or the recognition of real differences.

This holds true as well when we come to individual preferences for physical attributes such as height, weight, "richly" endowed body, hair color, and so forth: these are solely matters of individual taste. And given that there are individual preferences for or against physical attributes in general, we expect people to exhibit preferences for or against racial attributes as well. Indeed, so far as our analysis is concerned, there are no conceptual distinctions between racial and other preferences.

It may be rejoined that racial preferences are not comparable to other kinds of preferences in the consequences they have for society and for individuals. However, although the indulgence of racial preferences has specific effects that the indulgence of preferences for certain wines does not have, are the preferences basically different? If so, how do they differ? The preference for Bordeaux wines "harms" Burgundy producers by reducing the value of resources that are held for Burgundy production. If the consequences of preferences are generally to reduce the value of some resources and increase the value of others, then it can be said that preferences for physical attributes have effects similar to those of other preferences. The essential difference—by no means small—between preferences for racial features and those for wines is that the latter are not as specialized as the former. In other words, if Burgundy producers see that consumers prefer Bordeaux, they will try to shift their resources to Bordeaux production. On the other hand, for example, people who are black cannot become white.

But the fact that racial characteristics are unchangeable does not put them in a class by themselves. Persons with average IQs are preferred to those with below-average IQs, and persons who are not physically disabled are preferred to those who are. In each of these cases, the less-preferred characteristics are unchangeable and in each the less-preferred person suffers a competitive disadvantage. This disadvantage is to be expected. Disadvantage and advantage are inevitable consequences of differences in individual tastes, abilities, and traits, on the one hand, and of freedom of choice in a democratic society, on the other.

What I have said could be construed as trivialization of the problems of minorities and a defense of the status quo in racial matters—in which case it will necessarily offend the sensibilities of decent people. I do *not* consider the problems trivial, do *not* defend that status quo, and *do* personally find choices made solely on the basis of racial preferences obnoxious. However, in what follows, it will be shown that many racial outcomes are the results *not* of racial preferences per se but of political restraints on voluntary exchange. In a world

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where racial preferences are not the sole cause of these outcomes, policies that assume they are will fail.

Racial Prejudice. The term prejudice has the Latin root meaning "to judge before," and a prejudiced act may thus be defined as a decision made on the basis of incomplete information. (Note that prejudice, like preference, is not the act but the cause of the act.) Making decisions without complete information is necessary in a world of scarcity and uncertainty, and in a complex world erroneous interpretation of the available evidence is by no means uncommon. Moreover, different individuals may arrive at different conclusions even if confronted with the *same* evidence, and the behavior of any given individual may sometimes not respond to changes in the evidence.

Consider a simple example of how decisions are made on the basis of incomplete (and perhaps misinterpreted) information. If a fully grown tiger suddenly appeared in the room, most of us would rush for the door, not because of what we knew about that *particular* tiger but because of our stock of information—and misinformation—about tigers as a class. The response is based on a stereotype—that is, the individual makes a prejudiced decision. He makes no attempt to seek additional information, but rather ascribes known or surmised group characteristics to the individual tiger. Examples of prejudiced behavior abound—not talking to strangers, running in response to rustling in the bushes, not buying bent cans of food, not recruiting employees from certain schools, and so on.

Decisions to prejudge are inextricably tied to individual judgments on what constitutes optimal information search. Information is not a free good; it is acquired by the expenditure of time, effort, money, and income foregone. As a result, wealth-maximizing individuals can be expected to economize on information costs. For any of us there will be a point at which the cost of acquiring one more unit of information is equal to the expected gain from that unit—which means that further information will not be acquired because the added cost would exceed the expected added gain.

A vast number of decisions must be made during our lives. Some of them, such as deciding to greet a passerby in the morning, require relatively small amounts of information. Others, such as selecting a marriage partner, require relatively larger amounts. A person is not prejudiced or unprejudiced. Rather, a person *always* exhibits prejudiced behavior to the extent that he substitutes general information (prejudgment or stereotypes)—which is less costly—for more costly specific information. What distinguishes among people are their comparative degrees of prejudiced behavior when facing similar situations.

In the literature on racial behavior the word "prejudiced" is most often used pejoratively to refer to those whose optimum quantity of information is deemed by the observer to be too small. Behavior based on racial or sexual stereotypes is commonly viewed as making use of too little information and thus viewed as opprobrious—and in many cases, of course, it is illegal. However, the quantity of information effectively collected before decisions are made (which is the reciprocal of prejudice) is up to the individual's calculation—for there is no social standard or optimum amount of search that is applicable to all individuals in all cases. For example, for the prospective house buyer, there is no socially determined optimum number of houses to be looked at before making a decision. Instead, the amount of information collected by free individuals before acting is determined by and reflects, among other things, the efficiency of the individual in converting resources into information and the value of those resources as measured against the expected value of a "correct" decision.

Since all of us will seek to economize on information expense, we will substitute less costly forms of information collection for more costly forms. Physical attributes are easily observed and hence constitute a cheap form of information. If a particular physical attribute is highly correlated with some less easily observed attribute, then the physical attribute may be used as an estimator or proxy for the other. The cheaply observed fact that an individual is short, or an amputee, or a Negro, or a woman thus provides "sufficient" information for predicting the presence of some other unobserved attribute. Most of us, for example, if asked to identify individuals with advanced academic degrees *only* by observing race and sex, would assign a higher conditional probability that white males would have such de-

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grees than black males or women. Such behavior is what decision theory expects where *unobservable* variables must be estimated from *observable* variables.

Real Differences. Discrimination need not, of course, be based on preferences as the word is generally understood (that is, tastes) or on prejudice (that is, judging before all the returns are in). It may be based on virtually complete knowledge of real differences and have nothing to do with aesthetic (or other) sensibilities. My reluctance to remain in the room with an uncaged tiger is, though reasonable, prejudice—since it is virtually certain that my sample of tigers previously experienced is statistically insignificant. My reluctance to ride in a bus may be a matter of preference—taste—if it is based on the fact that I find buses, though cheap, aesthetically unappealing. But there are other kinds of choice, and though one may object to their being included under the general rubric of discrimination, it will be seen later on that acts based on full knowledge and rational calculation have been considered "discriminatory" in the bad sense.

My reluctance to remain in the room with an uncaged tiger is, though reasonable, prejudice—since it is virtually certain that my sample of tigers previously experienced is statistically insignificant.

Prejudice in Action

Some may think my discussion of discrimination and prejudice renders the words meaningless, since it can be said that all human acts involve choice and all choices are based on incomplete information (as well as on tastes). But the discussion is useful because it permits us to avoid confusing one form of behavior with another. It enables us to see that certain kinds of choices—those made on the basis of racial, sexual, and other physical attributes—may be intelligent optimizing or may be the result of tastes. An example will clarify these points.

Suppose we are on a university campus where the racial and sexual composition of the student body is the same as that of the U.S. population, and suppose we play a game of trying to identify students who can find the integral for the mathematical expression $\int x^2 dx$. Players are given zero information about the students' mathematical proficiency and may not communicate with students except to ask, What is the integral? In other words, players can distinguish between students *only* by observable attributes such as race, sex, mannerisms, dress, and speech accent. The game is played for money, and it is assumed that the player's objective is to maximize his winnings.

The player is in a situation where choices must be made on the basis of incomplete information. He is faced with identifying the observable attributes that will be the best indicators of student proficiency in calculus (the unknown and unobservable attribute). *If* he thinks that mathematical proficiency is equally distributed by physical attributes, his choice process will be essentially random. But if he thinks that mathematical proficiency is *not* so distributed, he must adopt a different (nonrandom) decision rule. In his first cut at such a rule, he may decide not to choose females because he knows that women are not well represented in the quantitative sciences. (Note that such a rule might not be as valuable in the Soviet Union, where a greater portion of women enter the quantitative sciences.) In successive cuts at a decision rule, the player may discriminate against — not choose — Negroes, Puerto Ricans, and American Indians, perhaps reflecting his awareness that math skills are related to the quality of pre-college schooling and that these particular minorities have historically received grossly inferior elementary and secondary education. In the end, the player may settle on a rule that confines his choices to males of Jewish or Oriental ancestry.

I am *not* saying that there is a genetic or causal relationship between race or sex and mathematical proficiency. What I am saying is that these variables are correlated in the real world (though I think it risky even to suggest possible explanations).

Suppose we relax the implicit assumption of neutral racial preferences and assume, instead, that the player has a distaste for Jews and Orientals but still believes these groups to be disproportionately represented in the quantitative sciences. So long as we retain the as-

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sumption that the player seeks to maximize winnings—that is, economic payoff—his decision rule, his prejudice, will not be distinguishable from that of a player with no racial preferences.

This illustrates an important point that is lost in most discussions of racial issues: choices made on the basis of race (or sex) do not always permit us to put the preferences of the chooser in unambiguous categories. Moreover, the example raises a question whether anyone should care if the player in the game chose to indulge his preference and *not* select Jews or Orientals? In our scenario (assuming that Jews and Orientals are disproportionately represented in the class of individuals knowing calculus), the player who because of tastes discriminated against Jews and Orientals would win less than other players. Even the most fervent advocate of civil rights would have little reason to seek a social policy that required anti-Jewish or anti-Oriental players to give Jews and Orientals an equal opportunity to be selected. The racist (or, for that matter, any individual who permitted his choices to be determined by economically irrelevant "preferences" of whatever kind) would bear the full cost of such an action. He would lose money.

Racial Preference, Optimizing Prejudice, or Real Differences?

For some reason these points tend to get lost in discussions of racial discrimination. We overlook the fact that not every discriminatory action reflects preferences—a dislike of Negroes per se, for example: certain discrimination may come from the rational behavior of individuals minimizing search costs or confronting real differences in the market, whether that market is free or institutionally constrained. And we overlook the fact that, in a free market, economically irrational preferences will—as in our hypothetical game—impose costs on whoever indulges them. Institutional restraints may, of course, render that indulgence costless to the indulger. If they do, the answer is to lift the restraints and reimpose the costs—in other words, to free the market.

When we are formulating policy, we must be careful to distinguish among the three sources of "discrimination"—preference, prejudice, and real differences. If we assume that racial tastes cause the problem we are addressing, when in fact the problem is caused by something else, our policy will be at least ineffectual and quite possibly harmful to its intended beneficiaries. Let us look here at three areas where whites are generally charged with discrimination against blacks, and where the assumption is generally made that the discrimination is based on racial preference—that is, tastes. These areas are hiring, home mortgages, and the prices ghetto shoppers pay.

Hiring and Employment Discrimination. Many recruitment and hiring practices are said to reflect racial preference, but an alternative explanation can be drawn from our knowledge of hiring procedures. When a firm seeks labor, it must find out how productive those seeking jobs are likely to be and must train the persons it hires. Since this process costs money, the firm has reason to search for recruits that appear to have a high probability of success. If the firm believes there is an important relationship between a recruit's high school performance (and the quality of his high school), on the one hand, and employee productivity, on the other, it can reduce some of its recruitment costs just by knowing the job candidate's record (and high school). If a firm knows that blacks at grade twelve are typically three to five years behind whites in scholastic achievement, it can assign a higher probability to a white recruit's having the desired productivity.

In the mind of the employer, skin color may be a first approximate indicator of expected worker productivity. To observe a process that selects in part by skin color and to attribute the selection to taste (in this case, to employer "racism") would be misleading. It would be like concluding that auto insurance companies charge drivers under twenty-five years of age higher premiums and that life insurance companies charge women lower premiums because these companies dislike young people and men. In both cases, a physical attribute may act as a general proxy for some other attribute (in the case of drivers, the higher probability of an accident) that is individually more costly to ascertain.

Suppose an employer who has racially neutral preferences *incorrectly* perceives that, on the average, a Negro worker is less productive

(Continues on page 46)

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than a white worker. What kinds of laws would cause him to seek more information and perhaps revise his perception? Clearly, laws that require him to pay all workers identical wages or that make it very costly to fire an employee have the opposite effect because they reduce his incentive to experiment. That is, employers will be less willing to hire someone of uncertain productivity if the wage must be the same as that paid a proven worker and if they are unable (or if it is costly) to fire that employee should hiring him have been a mistake.

In fact, some of the employment problems faced by blacks are quite certainly created by systematic institutional disincentives to hire them. One such disincentive is the minimum wage law, which now requires firms to pay an hourly wage of at least $2.90 no matter whom they hire. Thus, if prospective employees are undifferentiated except by race, an employer who has a distaste for Negroes may indulge this distaste at zero cost to him. On the other hand, if there were no wage-fixing arrangements and if a Negro worker were willing to offer a compensating differential (work for a lower wage), employers would suffer a positive cost if they based their hiring decisions on racial tastes alone. That is, they would have to forego the profits that they could have enjoyed from hiring the lower-priced worker.

The minimum wage law will produce adverse consequences for Negroes even if the racial preferences of the employers are neutral. Many people have tried to explain the unprecedented high rate of black youth unemployment (40 percent) relative to that of white youth (16 percent) by claiming racial bias (what we are calling preference). But in 1948 black teenage unemployment (9.4 percent) was *lower* than white teenage unemployment (10.2 percent), and up until 1954 the labor force participation rate of black youth *exceeded* that of white youth. Certainly this dramatic reversal has not come about because the nation's employers have become more racist since the 1940s. Rather, it is the minimum wage that is the culprit. Firms will not choose to pay the minimum wage to workers whose hourly output is less than the minimum—which, given the law, means they will not hire them—and youths, especially minority youths, tend to have hourly outputs worth considerably less than $2.90.

The basic characteristic that the minimum wage law shares with many other laws is that it prevents people from offering compensating differentials to offset nonpecuniary differences—that is, from selling at a lower price or buying at a higher price. When there are laws that set prices and prevent voluntary exchange, less preferred people tend to be made worse off. Consider what would happen if less preferred painters were not permitted to compete in selling their paintings by charging lower prices, or less preferred doctors (interns) to compete with more preferred doctors by accepting lower wages. Institutional restraints of the sort represented by controls on prices predictably decrease price competition, which in turn means that personal (nonprice) attributes play an increased—indeed, dominant—role in choice.

Not hiring blacks may be described as "prejudice" if employers are simply economizing on information costs by accepting a stereotype whose roots are real but whose ultimate accuracy is a matter of conjecture. Or—especially in the case of black youth—it may be described as a simple recognition of real differences. But in either case, the failure to hire could be rectified (or at least substantially ameliorated) by abridging the requirements of laws regulating wages—a point that seems finally, hesitantly, tentatively, to have taken root in the minds of members of Congress, so far as those laws touch teenage workers.

Home Mortgage Discrimination. The situation is similar with redlining, a practice whereby banks and similar institutions refuse to grant mortgages for homes in certain neighborhoods. Because the practice most often applies to minority inner-city neighborhoods, the national debate about it has focused on its racial aspects, with banks being labeled as racist.

Forgotten in much of the debate is the existence of regulations that place ceilings on the interest rates banks can charge for home mortgages. Given these ceilings, banks have an incentive to ration credit—that is, to lend money to those whose perceived credit worthiness is appropriate to the permitted interest rate. It turns out that, for a number of reasons, the probability of default per dollar lent is greater in some neighborhoods than in others. Moreover, several laws designed to protect borrowers make the collection and eviction of debtors

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who are in default more costly to bankers. These circumstances reduce the probability of earning normal profits in some neighborhoods.

Thus, redlining need not be a result of bankers' racism. In many cases (perhaps almost all), it occurs not because bankers are unwilling to make home loans to inner-city blacks but because the inner city is not a profitable market at the state-imposed interest rate ceiling. The real villain in the redlining issue is the legislature that imposes, say, a 10 percent interest rate ceiling. Such a ceiling in effect says that if an applicant is not a good enough risk for a mortgage at 10 percent, he will not get a mortgage at all—though without a ceiling he may get a mortgage at a 15 percent rate. Interestingly, *black*-owned banks that do not find the ghetto an attractive place to make loans are not called racist, and we should note that most black-owned banks invest more of their loan portfolio *outside* the community in which they are located than do white-owned banks.

Public policy directed at supposed banker racism will miss its mark and may, like affirmative action in lending, exacerbate the credit problems of blacks. Banks will simply move away. An effective policy would examine cost conditions in inner-city ghettos and remove or ameliorate state usury laws. Once again, what is prejudice or perhaps a recognition of real differences is misdiagnosed as "preference"—with predictably poor results.

Discrimination against Poor Shoppers. During the mid-1960s it was widely alleged that white merchants in ghetto areas expolited their customers by charging higher prices and selling lower-quality merchandise there than they did elsewhere. The merchants, it was said, were trying to earn supranormal profits as a way of acting out their racial hostility toward Negroes. But it turns out that what was involved was not preference or even prejudice.

Prices were indeed higher in ghetto areas, and several studies showed that retail food chains followed different pricing policies in ghetto and nonghetto areas. With these findings in hand, the Federal Trade Commission along with consumer advocate groups and public interest lawyers attempted, through public pressure, to require that ghetto merchants offer their customers the same terms of exchange that were offered in nonghetto areas.

But to view the merchants' behavior as exploitative or racist ignores the fact that ghettos tend to present a high cost business environment. Losses from business-related crime are higher there than elsewhere *as a percentage of total sales*; business, fire, and theft insurance premiums are also higher; and extension of credit is riskier. In addition, because of the low income of ghetto residents and its effect on sales mix and volume, merchandising techniques used to lower sales costs in nonghetto areas are not readily adaptable to ghetto areas. In other words, much of the behavior that the critics condemned is merely an economic response to an environment that raises the cost of doing business. If products and services are to be provided in the ghetto, prices must reflect these higher costs.

Evidence substantiates this explanation of merchant behavior. The Federal Trade Commission has shown that while gross margins were higher in ghetto areas, the difference was *more than* accounted for by higher operating costs, and the return on equity was considerably lower in the ghetto than elsewhere. The assertion that supranormal profits were earned becomes even less credible when we recognize that retailing is characterized by relative ease of entry, so that if supranormal profits existed, merchants would open new businesses until profits in ghetto and nonghetto areas were equalized. The opposite of this has occurred in urban areas: businesses have left without being replaced. Furthermore, none of those who attributed the prices charged by white merchants to racism noted that the prices charged by Negro merchants were about the same.

The crusade that blamed the problem of the ghetto consumer on the greed and "racism" of whites, may well have reduced the welfare of the ghetto consumer. The adverse publicity and boycotts (and other actions) against merchants in ghetto communities gave these merchants increased reason to move out. The result is fewer neighborhood stores, with shoppers being forced to travel longer distances or pay even higher local prices than in the past.

Clearly a policy designed to aid the ghetto consumer would emphasize ways to improve the business environment. It would, among other things, permit lower wages and provide interest subsidies, while recognizing that efforts to reduce the costs of doing business in

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ghetto areas will fail in the absence of strict law enforcement to reduce crime.

Conclusion

The difficult problems faced by racial minorities are made even more difficult by their intertemporal aspect—the fact that the present-day disadvantages of blacks and other minorities are inextricably tied to the injustice of the past when they were denied even the most minimal constitutional guarantees. But to acknowledge that today's difficulties have a long history does not tell us what the proper and effective remedies would be. Upon what working principles should they be built? And what might these remedies do to the values of a democratic society? He who says that blacks should be given a competitive *advantage* in the market is, of necessity, also saying that others should be given a competitive disadvantage. This philosophy says in effect that D must compensate C because of what A did to B in some other generation—surely a strange system of justice and a dubious basis of social order.

This is precisely the case with the racial quotas imposed because firms and schools are believed to have been indulging racial preferences in hiring and in admissions. Aside from the equity issues that can be raised, quotas raise other issues as well. If, instead of racial bias, the behavior is rational discrimination in the face of imperfect and costly information, a quota policy completely misses the underlying cause of the behavior—namely, the poor education received by most blacks or the market credibility of their education certificates. But the harm caused by quotas is not limited to focusing attention on the wrong problem. Forcing firms and schools to have racial quotas that may be independent of worker or student qualifications aggravates racial hostilities, reinforces racial stereotypes, and (perhaps most destructive) creates debilitating and sometimes false expectations for young Negroes—expectations of ascribed (as contrasted to achieved) status that are, moreover, realistic only where and to the extent that "affirmative action" prevails. And, given the trend of recent court decisions, affirmative action may have heard its death knell.

Many Americans condemn racial quotas as a violation of democratic principles. But the matter is not so easily dismissed, for the reason that the economic game is not being played fairly. A wide variety of national and state policies—laws setting minimum wages, the national labor law fostering union monopolies, occupational and business licensing laws, and regulatory laws like those administered by the Interstate Commerce Commission—discriminate against whole classes of individuals. Specifically, they discriminate against latecomers, against those without political clout, against those having little skills and capital—which means, almost by definition, disadvantaged minorities. Therefore (as just one example), given that we have laws in effect requiring membership in a union local as a criterion for employment and given that some union locals find ways to restrict minority membership, quotas may be a "second best" way of giving minorities job opportunities in the trade. The first best solution would be to eliminate the government-supported monopoly. Certainly those who find racial group membership an offensive criterion for employment should find union group membership equally offensive.

The basic problem that blacks now face in the United States is not one of malevolent racial preferences per se, though it may have been that in the past. It is, rather, one of government restrictions on voluntary exchange. These restrictions arise because powerful political groups are able to use the coercive powers of government to subvert market competition, to eliminate the relative parity of the marketplace, and to make rules that redistribute wealth in their favor. To the extent that emotionally charged words such as exploitation and racism are to have an economic meaning, they should refer to the myriad of collusive agreements, backed by government, whereby disadvantaged minorities are subjected to a continuing disadvantage. ■

The basic problem that blacks now face in the United States is not one of malevolent racial preferences per se. . . . It is, rather, one of government restrictions on voluntary exchange.

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How Smoking Increased When TV Advertising of Cigarettes Was Banned

Gideon Doron

THE U.S. DISTRICT COURT for the District of Columbia ordered major cigarette manufacturers on January 25, 1979, to turn over to the Federal Trade Commission data on the effects of advertising on cigarette sales. Meanwhile, there are reports that the FTC is considering (informally) the possibility of going back to the old days of anti-cigarette ads on TV—the "anti" ads having gone off the air with the "pro" ads eight years ago. The current situation prompts a look at one of the neater examples of industry's using regulation for its own purposes.

In 1970 Congress passed an advertising prohibition act banning all cigarette commercials from the broadcast media effective January 2, 1971. The ban was expected to decrease cigarette smoking, the assumption being that the commercials induced people, particularly young people, to take up the habit and also that the "public service" anti-smoking ads were ineffective. But the expectation was not met: indeed, cigarette consumption, which had been declining before 1971, began to increase.

In fact, not only was the original prohibition fully compatible with the self-interest of the tobacco industry, but its benefits to the industry were predictable long before the act was implemented. And, as we will see, they were actually predicted, but not so widely that enough members of Congress caught on.

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Regulating Cigarettes

While health complaints against the practice of smoking had been sounded long before the 1960s, it was the release of the surgeon general's report in January 1964 that put the issue on the public agenda and made cigarettes subject to new forms of government regulation. The anti-smoking coalition that emerged after the report was led by the Federal Trade Commission (FTC) and the Federal Communications Commission (FCC). Both concentrated primarily on the nature and content of the information transferred by the industry to its customers through advertising. As a result of the coalition's activities, three major regulations emerged.

First, the Cigarette Labeling and Advertising Act of 1965 (P.L. 89-92) required a health warning label on each cigarette package effective January 1, 1966. In 1971 a health warning label was also required in each cigarette advertisement. Second, the Fairness Doctrine, as embodied in section 315(a) of the Communications Act and as newly interpreted by the FCC in 1967, guaranteed free broadcasting time to anti-smoking forces and provided public assistance for the filming of those anti-smoking commercials. These commercials were aired during the years 1968–70 at an estimated cost of $50 million worth of broadcasting time each year. Third, the Public Health Cigarette Smoking Act, enacted in April 1970, prohibited television and radio commercials for cigarettes effective January 2, 1971 (P.L. 91-222).

While the release of the surgeon general's report and the immediate controversy that surrounded it had been followed by a reduction of about 4 percent in the total consumption of cigarettes, the labeling act had no significant effect. (After all, by 1966, most smokers were aware of the health risks they incurred by smoking.) It was, in fact, a boon of sorts to the

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industry, now legally protected by the warning label against potential liability suits for damages to health arguably caused by cigarettes.

The effects of the other two regulations are of greater importance. To understand these, we should first analyze the objective of cigarette advertising.

The Role of Cigarette Advertising

The cigarette industry consists of six major firms—their familiar historic names being R. J. Reynolds, Philip Morris, American Tobacco, Brown and Williamson, P. Lorillard, and Liggett and Myers—and several smaller ones. The industry is an oligopoly in which these six firms control over 99 percent of the market. But the "special" feature of this oligopoly (distinguishing it from many other oligopolies) is that prices are inflexible downward because costs are largely determined by outside forces, including government. Essentially, the tobacco firms cannot lower the prices of cigarettes unless taxes are lowered or unless the amount of tobacco in a cigarette is reduced (on which more later), or unless the price of tobacco is lowered. That is, most of the costs to cigarette manufacturers are beyond their control; and with no additional economies of scale likely and profit per package around one-and-a-half cents, the firm would have to cut this profit by 66 percent in order to produce a one-cent-per-pack reduction for the consumer. This is unlikely as well as unattractive.

This is not to say, however, that firms in the industry do not compete against each other. They do indeed, but their competition is for the most part competition by advertising, and it is advertising that the government decided to regulate at the beginning of the 1970s. The prime objective of cigarette advertising is not to generate new demand—that is, convincing nonsmokers to smoke—but rather to convince smokers to experiment with another brand at the expense of the brand usually smoked. This was plainly stated by Frank Saunders, top executive of Philip Morris Tobacco Company, who told *News and Observer* in October 1971 that "TV advertising was never designed to create new smokers" and that "it's main purpose was to switch people from one brand to another. . . ." To put the matter another way, cigarette firms use advertising as a tool for competition over market share and not for market expansion. It follows, then, that by impairing the ability of all firms in the industry to advertise their product, the government would be reducing the scope of their market competition (an outcome incompatible with the public interest). But the size of the market need not be affected.

Anti-advertising, on the other hand—advertising against smoking—reduces the size of the market. This is because, if all other things remain the same, consumers making their decision as to whether to buy cigarettes will take into consideration the new unfavorable information and may choose to alter their consumption patterns. In particular, those who smoke less than a pack a day (the "marginal smokers") may be "talked into" quitting by the anti-smoking commercials.

During the seven years from 1964 through 1970, unfavorable information was transmitted to the public first by media coverage of the controversy (1964 through 1967) and then by media coverage *and* direct anti-smoking commercials under the Fairness Doctrine (1968 through 1970). Over the entire period, per capita consumption of cigarettes for the population fourteen years old and over went down by an average of 1.6 percent a year. Over the last three years, with the "anti" ads, it went down by an average of 2.6 percent a year. This, of course, was unpleasing to the industry. In order to maintain their shares in a shrinking market, cigarette manufacturers engaged in fierce advertising competition. As a matter of fact, the industry as a whole increased its average annual spending on advertising by over $60 million (by 50 percent) from 1956–63 to 1964–71.

Since advertising does not necessarily contribute to market expansion . . . and anti-advertising does contract market size, it would obviously be in the industry's interest to bring about the elimination of both. . . .

High expenditures, low sales, and consequent decreased profit is something every industry tries to avoid. Since advertising does not necessarily contribute to market expansion for

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the cigarette industry and anti-advertising does contract market size, it would obviously be in the industry's interest to bring about the elimination of both forms of advertising. This was accomplished by the prohibition act of 1970.

The Effects of Prohibiting Advertising

Apart from reducing the level of competition among firms, the prohibition benefited the industry in other interesting ways.

First, it ended the application of the Fairness Doctrine to cigarettes. In essence the Fairness Doctrine requires that when a station allows its facilities to be used for the presentation of one side of a controversial issue, it must see that the other side is presented as well. The doctrine—which has its roots in a 1929 decision of the Federal Radio Commission—was intended to guarantee fair presentation of opposing political views. Its 1968 application to cigarette advertising established what many saw as an alarming precedent for numerous industries whose products might be called into question by consumer groups. However, since the justification for applying the doctrine to cigarette advertising was grounded in the fact that smoking (a controversial issue) was being encouraged by advertisements, the FCC could not require "equal time" in the absence of cigarette commercials. (One thing the FTC is reported to be considering now is a tobacco-industry-supported fund to pay the costs of anti-smoking ads, which gets around this problem.) Ending anti-smoking commercials removed the major factor contributing to decreased cigarette consumption. It is not surprising, then, to find that total sales of cigarettes showed an average annual increase of 2.5 percent in the five years following the advertising ban, the greatest increase being 4.4 percent in 1973.

Second, the prohibition saved the industry money. Despite increased advertising outlays in the unregulated print media, the industry's overall advertising expenditures were $80 million lower in 1971 than in 1970, and in the next five years were still significantly lower than their average for 1964–71. The savings presumably were incorporated in the funds used for general diversification.

Third, with TV and broadcast advertising banned, the six major firms acquired an almost lasting control over the market. Without national advertising it is difficult in the extreme for new firms to enter the cigarette market. Erection of barriers to entry is generally believed to be a major objective for an industry in negotiating regulation. (Another objective is of course acquisition of direct subsidies, which tobacco growers receive through the agricultural tobacco support plan, but this is beyond our present topic.)

Finally, the ban and the controversy that preceded it helped the industry by substantially reducing cigarette production costs. As a result of alterations in consumer taste in favor of "safer" cigarettes, all firms are currently offering low-tar and low-nicotine cigarettes. Even before the ban on advertising, it had been estimated (by *Advertising Age*, December 1, 1969) that such brands contained 50 percent less tobacco than previously popular cigarettes, so that it could be predicted the "safer" cigarettes would be more profitable to the manufacturers. With the industry heavily promoting these cigarettes through the unregulated print media, the market share of these brands (those with fifteen milligrams of tar and under) increased from less than 1 percent in the late 1960s to about 16 percent in 1976—and is still increasing—at the expense, of course, of the older brands. The FTC requires that information about tar and nicotine content be placed in all cigarette advertisements, but this regulation, which emphasizes only two known components of the product (ignoring many others that may be detrimental), may actually create a false sense of safety among smokers. Recent findings on carbon monoxide in low-tar and low-nicotine brands cast doubts on the reasonableness of this requirement—but that is another story.

The irony in the situation is that the increased level of consumption after 1971 is attributed, in part, to these "safer" cigarettes—not only because they are "safer" but also because they are so mild that smokers wind up smoking more in order to receive the same nicotine payoff. Furthermore, after 1971, younger people began to smoke in increasing numbers. This was revealed in a study conducted in 1976 for the American Cancer Society, *Teenage Boys and Girls and Cigarette Smoking*, which concluded that "most teenage boys and girls now start to smoke before they are in junior high."

The objective of the prohibition was, as expressed by Senator Frank Moss (Democrat,

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Utah) in the congressional debate in 1969, "mainly . . . protecting young people who had not yet begun to smoke but were subject to powerful inducements to smoking via television advertising of cigarettes." The growing numbers of kids who began to smoke without being exposed to cigarette advertising on television points to the prohibition's serious failure to meet its objective.

Accident or "Conspiracy"?

It is at least arguable—and I think virtually certain—that the cigarette industry has thrived not in spite of this particular public regulation but because of it. Was this development the accidental effect of the regulation or was it intended?

Clearly, the industry was aware that bans on cigarette advertising in other countries had not worked against the tobacco companies. In Italy cigarette sales increased by 3.5 percent after an advertising ban was imposed in 1962, and in Great Britain the average annual increase was 3 percent after the ban of 1965. The steady annual growth of sales for the U.S. liquor (not the beer) industry, which does not advertise its products on television, would also have been an indicator that lack of television advertisement would not necessarily harm the tobacco industry.

These points surely had not been overlooked. For example, in 1968, before the regulatory agencies and Congress took steps against cigarette commercials, Smith, Barney and Company (members of the New York Stock Exchange) sent out an investment report on the significance of a possible ban of cigarette advertising on television and radio. The report concluded that the cigarette industry had an incentive to discontinue its commercials voluntarily and that discontinuance would free large sums of money to support acquisitions and diversifications and lead to increased earnings. Had the ban taken place in 1968, it was estimated, the increase in that year's earnings per share of common stock would have ranged from roughly 25 percent (R. J. Reynolds) to over 60 percent (Liggett and Myers and P. Lorillard).

Equipped with this knowledge, Joseph F. Cullman III, chairman of the Tobacco Institute Executive Committee (in a statement to the Senate in July 1969), offered to discontinue cigarette ads in the broadcasting media by September 1970 at the latest, when "major" contractual arrangements for air time would expire. He also said that advertising could end sooner if the broadcasting industry would agree to cancel existing contracts simultaneously at any point after December 1969. (The only condition attached was a congressional waiver from antitrust laws since such communal withdrawal might be considered a collusive act on the part of the manufacturers.) The industry *rejected* a plan offered by the National Association of Broadcasters to phase out cigarette commercials gradually over a four-year period beginning on January 1, 1970, and rejected the date proposed by the FTC (which was 1971).

In this light, it is not surprising to find strong views expressed in the House of Representatives against the prohibition bill. For example, Brock Adams (Democrat, Washington), John D. Dingell (Democrat, Michigan), and John Jackman (Democrat, Oklahoma) jointly called the bill "sweeping carte blanche protection for a particular industry." Bob Eckardt (Democrat, Texas) expressed the opinion that the bill "would cut off debate on the hazards of smoking"—which it apparently did.

The industry did not, in this instance, capture the regulators—but it did, and designedly so, capture the regulation.

Members of the anti-cigarette bloc in the House never numbered more than forty, which would strongly suggest that any law the Congress passed would not be what they wanted. But they hailed the Public Health Cigarette Smoking Act as a major victory, whereas they had, in fact, been defeated. If public interest was to be harmed by an increase in smoking, then public interest was not served by this public regulation. Government moved, with predictably poor results, from providing information (which it does reasonably well) to regulating by fiat. The industry did not, in this instance, capture the regulators—but it did, and designedly so, capture the regulation.

One finds a certain sympathy for the FTC. ■

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Readings
of particular interest

How Society Makes Life and Death Choices

Tragic Choices by Guido Calabresi and Philip Bobbitt (New York: W. W. Norton and Co., 1978), 252 pp.

"Tragic choices" are a society's decisions allocating certain scarce resources—those resources that involve life itself. Each society makes these decisions in different ways, based on its own traditions and values. Guido Calabresi of Yale Law School and Philip Bobbitt of the University of Texas Law School set out to examine these processes and thereby to illuminate the character of the societies described—because "it is in the choosing that enduring societies preserve or destroy those values that suffering and necessity expose." The choosing is in two stages—"first-order" decisions (how much of a good should be produced?) and "second-order" decisions (who gets the good?). Calabresi and Bobbitt concentrate on population policies, conscription policies, and access to kidney dialysis machines as examples of society's "tragic choices."

Resources can be allocated through the "pure market," through the democratic political process, through a lottery, or by custom (in which case the allocation evolves instead of resulting from conscious choosing). The authors criticize pure market allocation because it does not take account of social goods, because it contradicts some important views of egalitarianism, and because it too openly prices goods that society considers priceless. Allocation through the political process poses problems by openly involving the entire society in the act of preferring some persons to others in life-and-death decisions, seemingly in conflict with basic ("unalienable") rights. Although lotteries embody the principle of absolute equality, they contradict other views of equality (like the American belief called here corrected egalitarianism—based on the formal principle that discrimination is permissible if "likes are treated alike," so long as the results do not link acceptable categories of discrimination with unacceptable ones like wealth or race). Lotteries also expose too clearly society's unwillingness to provide enough for all in need to have the good. Finally, the authors criticize allocation by custom because, by pretending no choices are actually being made, it destroys honesty and openness—societal values as important as equality or the sanctity of life.

The authors point out that the "object of public policy must be . . . to define, with respect to each particular tragic choice, that combination of approaches which most limits tragedy and which deals with that irreducible minimum in the least offensive way." They discuss various mixed approaches—among them, the jury and its analogs (devices that try to avoid the defects of open political allocation by giving results without explanation) and several inventive market modifications. Calabresi and Bobbitt first stress the importance of historical perspective (how a society dealt with a tragic dilemma in the past) as a constraint on the choices that can now be made. Using conscription policies as an example, they show that in the American experience every sort of allocation device has been used to recruit soldiers when the country's manpower needs have not been met.

Next they emphasize culture as an influence both on what is regarded as tragic and on how it can be appropriately dealt with. To illuminate this point, they first discuss U.S. population policies and then compare Italian, English, and U.S. approaches to allocating kidney dialysis machines. In the latter discussion the purpose is to "suggest how different conceptions of equality interplay with different institutional and legal traditions to make some approaches to tragic choices plausible for a society while excluding others." In spite of ini-

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tial contrasts in the means used by the three societies to allocate this scarce good, all ultimately have made a similar "first-order" decision—to attempt to accommodate every reasonable candidate for a kidney, even though this decision effectively valued the lives of renal failure victims more highly than those of sufferers from other diseases.

Human Health and Environmental Priorities

The Environment, Technology and Health: Human Ecology in Historical Perspective by Merrill Eisenbud (New York: New York University Press, 1978), 368 pp.

Merrill Eisenbud, director of the Laboratory for Environmental Studies at the Institute of Environmental Medicine, New York University, identifies three fundamental mistakes of the modern environmental movement: "lack of historical perspective, improper assignment of priorities, and attempts to do too much too soon." He argues that no one party is responsible for the present chaos in the environmental field. Instead, "industry, organized science, the Congress, agencies of the executive and judicial branches of government, the media, and the general public have all contributed. . . ."

Eisenbud takes up his subject in three parts—(1) the history of the human environment and environmental reform, (2) population size, food, energy, and raw materials, and (3) contemporary environmental issues—with a concluding appraisal of the environmental movement and the problem of human health.

In Part I the author points out that the modern environmental movement reflects the perspectives of those who make up its leadership—the economic elite, which puts "high priority on clear skies, clean water, and green space." Eisenbud contrasts these concerns with concerns for the living environment of the disadvantaged (for example, their rat- and roach-infested homes) or with the "misplaced emphasis" on tailpipe emissions rather than on the more serious problems of auto congestion and traffic accidents. Modern technology has produced many undesirable by-products at the same time that it has brought "intellectual and material privileges to ordinary people." The hostility of many in the environmental movement to technology ignores the essential role technology plays in environmental adaptation. "Only in the last few hundred years has technology begun to release us from enslavement by an environment in which we are at a disadvantage in so many respects." He describes the history of land abuse, the ecological dimensions of communicable diseases, and the development of public environmental policy.

Explaining the focus of Part II, Eisenbud says that a "proper balance of population size in relation to food, energy, and natural resources is basic to a sound relationship with the environment." He emphasizes the lavish amount of energy now used to produce food in the United States and the fact that producing food for the world at this energy use level would leave no petroleum for other purposes.

Part III, the major part of Eisenbud's study, takes up the subject of "environmental toxicology" and human health. He observes that even extensive animal testing cannot always tell beforehand what the effect of a new industrial chemical will be on humans. For example, vinyl chloride's capacity to produce a rare liver cancer in humans did not appear at all in animal tests, nor for many years in industrial workers. Although 60 to 90 percent of cancers are caused environmentally rather than genetically, Eisenbud emphasizes that personal habits such as cigarette smoking and alcohol consumption are included in environmental causes. In fact, cigarette smoking is "almost totally responsible for the increase in cancer mortality in the United States in recent years." The evidence thus far does not indicate that "cancer is predominantly due to air and water pollution or to cancer-producing substances which we add to our foods." And the increase in the death rate from cancer among persons seventy or older is not because of greater susceptibility but because the cancer-causing agents have had longer to work, now that other causes of death have been eliminated.

Among recent environmental issues of interest, Eisenbud discusses DDT (in thirty years of use there is no evidence that it contributes to liver cancer in humans as it does in laboratory animals), the automobile (which *itself*, rather than its tailpipe emissions, ought to be controlled because of the "congestion, noise, and death and injury by accident" it causes), and

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nuclear power (an Environmental Protection Agency study estimates that by the year 2,000, with several hundred nuclear reactors in use, the average dose received by the U.S. population will be ".0002 rem per year, or about .2 percent of the dose from natural radioactivity.")

According to Eisenbud, the reorganization of relevant federal agencies that occurred in the mid-60s following increased public interest in the environment drove many well-trained professional environmentalists out of government, their places being filled by impatient and inexperienced scientists, lawyers, and public-spirited citizens. In addition, responsibility for environmental health was removed from health agencies and placed in agencies that had been primarily concerned with wildlife and land management. As one consequence, the ban on DDT as a public health hazard was based on the arguments of professional environmentalists, not of health specialists.

The author calls for a "realignment of environmental health priorities," and criticizes the immense expenditures projected for air and water pollution control because of the minimal effect they will have on human health. Although he emphasizes instead the need to influence human behavior (to prevent smoking and excessive alcohol consumption) and to improve conditions in our cities (more concern for the environmental problems of the poor), Eisenbud praises the passage of the National Environmental Policy Act and the Toxic Substances Control Act, among others. These measures may make it possible "for society to enjoy . . . the benefits of new technological development with confidence. . . ."

Modern Regulation Begins

"Factory Regulation: A Reinterpretation of Early English Experience" by Howard P. Marvel, in *The Journal of Law and Economics*, vol. 20 (October 1977), pp. 379-402.

In Great Britain, the Factory Act of 1833 "marked the beginning of economic regulation as we know it today." The act banned textile industry employment of children under nine and restricted hours and working conditions for those under eighteen. For the first time enforcement was effectively provided for, with factory inspectors reporting to an office in the central government. Economist Howard Marvel of Ohio State, questioning the traditional interpretation that the act was meant to protect helpless young workers from rapacious textile entrepreneurs, attempts to show instead that the act was "designed to further the interests of a class of important textile manufacturers."

Marvel explains that, although there are insufficient data to show whether these intentions *succeeded*, the true *purpose* of the act was to restrict output, thereby raising prices and increasing the profits of those manufacturers least affected by the bill. These turn out to be the owners of the larger, urban steam-powered mills. By contrast, the mills most affected were the smaller water-powered mills, which were more subject to the vicissitudes of nature and more constrained by the new act from making up for them. Under the act, time lost because of dry spells or floods could not be made up by lengthening the working hours of children. Marvel found that those mills using water power employed more children, thus supporting his hypothesis that the act was meant to have a differential impact on different varieties of textile manufacturers.

Using both historical evidence and economic calculations, Marvel shows that the usual interpretation fails to account for the timing and the politics surrounding passage of the act and for its apparent effects. The Factory Act was passed after the Reform Bill of 1832 had increased the political representation of the Whig manufacturing districts at the expense of Tory landowners. "It is difficult to understand why the newly strengthened manufacturers . . . would now capitulate to the outcry for reform by passing a bill inimicable to their own interests." One clue is the pattern of response to the bill: support from a number of large manufacturers, such as the Manchester cotton entrepreneurs, and opposition from many other manufacturers — almost all of the Scottish mills, for example (wholly water-powered)— and from the factory workers themselves.

On the basis of research by Gavin Wright on the British textile market, and on additional data, Marvel shows that output restrictions by water-powered mills (as a result of the act) would have increased prices for steam-produced textiles. A 5 percent increase in the profits of those mills least affected by the new act

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would then have been possible. Marvel also tests his hypothesis on the probable selective burden of the act—that more cases would have been filed and higher fines levied against owners of water-powered mills in smaller manufacturing districts with relatively little political power than against the larger owners. Multiple regression estimates indicate that water-powered cotton mills "bore the brunt of enforcement activity under the Act," and that this enforcement included, typically, more separate violations and charges involving stiffer penalties than in the case of mills in steam-powered districts—further supporting the selective impact hypothesis.

Combining this with the political evidence, Marvel concludes that the Factory Act of 1833 was "intended by the leading textile manufacturers to restrict output," thereby raising prices and increasing the profits of the steam-powered mill owners at the expense of the water-powered manufacturers dependent on child labor.

Why States Regulate Electric Utilities

"The Demand for State Regulation of the Electric Utility Industry" by Gregg A. Jarrell, in *The Journal of Law and Economics*, vol. 21 (October 1978), pp. 269-295.

"The electric utility interests were not acting suicidally when, around 1910, they became the main champions of the movement for state regulation," according to economist Gregg Jarrell of the University of Rochester. He sets out to demonstrate this conclusion, thereby challenging the view that state regulation of electric utilities served the public interest by minimizing the power of natural monopolists and holding down prices and profits. To start with, regulation of the electric utility industry mostly took the form of special franchises issued by municipal governments, but between 1910 and 1914 twenty-seven states effectively eclipsed local control by creating state regulatory commissions with power over prices, entry, and services. Jarrell argues that the change was made "primarily in the producers' interests."

The theoretical justification for government regulation of the electric utility industry was that utilities were natural monopolies (such that economies of scale would finally permit only one firm to exist) and hence the market would fail, remediable only by state regulation. Municipal regulators—corrupt, confused, and unprofessional—would be replaced by well-paid and well-educated state regulators. Presumably lower prices, profits, and increased output would result from "effective" regulation.

In order to identify some sources of the demand for state regulation, Jarrell constructs a model that views regulation as a political commodity and assumes that regulators behave so as to achieve maximum political support. His results show that these sources include the size of the existing market surplus and the way that surplus is distributed before state regulation, which essentially depends on the competitiveness of the situation resulting from local regulation. A significant hypothesis implied by assuming that regulation is a political commodity is that prices and profits should *rise* after the commencement of state regulation. This hypothesis Jarrell tests empirically using data for three years—1912 (before adoption of state regulation in over half of the states), 1917 (after regulation), and 1922. Prices, profits, and output are compared for states that regulated early, by 1917 (ER), and states that switched to regulation later (LR). The results of this comparison indicate that regulation came earliest (which means the demand for it was greatest) in states with a more competitive market for electricity, that increases in price and profits in ER states just after state regulation began suggest that the effective demand for regulation came from utility producers, and that "the intensity of this demand . . . depended upon the utilities' profits under municipal regulation."

This view implies there will be greater demand for regulation where the market is larger. If this is the case, the ER states should be those where demand is high or the cost of producing electricity low, or both. Jarrell found that, on average, demand in ER states exceeded demand in LR states for all the years tested, and also appeared to grow more rapidly than did demand in LR states. Jarrell's findings provide support for questioning the soundness of the natural monopoly theory itself. It may be, he says, that the "franchise competition of municipalities was an effective means of regulation." In other words, "if the free-entry policies of some municipalities resulted in competitive

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prices in the electric utility industry with its important economies of scale," then doubts are raised about the conventional wisdom that the "market will perform inadequately in 'naturally monopolistic' industries," necessitating regulation to protect the public interest. Instead, state regulation apparently shielded private utilities from the "competitive policies of municipal regulators."

Tactics for Reducing Prices

"Federal Government Initiatives to Reduce the Price Level" by Robert W. Crandall, in Arthur M. Okun and George L. Perry, eds., *Curing Chronic Inflation* (Washington, D.C.: Brookings Institution, 1978), pp. 165-204.

There is general agreement that what Robert Crandall of Brookings Institution here describes as "government's varied microeconomic policies" have considerable effect on prices. Although no similar consensus exists about how to control inflation and maintain high employment and economic growth, Crandall suggests that government ought to explore ways to lower prices by using a "variety of basically microeconomic policy decisions." His target here is "indirect taxation," wherein government imposes costs on the production and consumption of goods (sales, excise, and payroll taxes, government regulation, and the like) rather than directly taxing individuals (income tax). He focuses on six major areas of government activity and argues that costs (and, thus, the price level) can be reduced by relying on direct methods of financing government programs.

Crandall argues that the greatest potential for reducing consumer prices rests in two areas —altering social security financing and altering sales and excise taxes. It is generally agreed that the employer contribution to social security is reflected in higher product prices (since labor costs are increased). He suggests shifting the financing of the disability and health insurance components of social security from the payroll tax to general revenues, and estimates that the resulting reduction in labor costs would shave 0.7 percentage points off the price level. As for sales taxes, Crandall demonstrates that offering federal grants to states would reduce their sales taxes by up to 2.0 percent of personal income. This would reduce the price level by 1.6 percentage points without bringing about a major redistribution of wealth among states. Moreover, if the government replaced federal excise taxes (for example, taxes on alcohol and tobacco) with income taxes, another percentage point could be taken off the measured inflation rate.

Four other possible changes attract Crandall's attention, though their effect on the price level would be less than that of the two already mentioned. First, programs that support farm prices through acreage controls and output limitations serve "to maintain the incomes of all farmers—particularly large farm operators." A wiser policy, Crandall concludes, would stress *income* supports to help the smaller struggling farmers in periods of low farm income. Such a shift would lead to a 0.5 percentage point decline in consumer prices.

Second, regulatory reform would also lower consumer prices. Among various options Crandall discusses are deregulating transportation (trucking and coastal maritime), replacing technology-specific regulations with goal-oriented regulations, and forcing regulators to monitor (and limit) the private resources devoted annually to compliance with an agency's regulations. To accomplish the latter, he proposes a "shadow budget" that would, in a sense, make regulators explicitly responsible for the private resources they "spend." Administrators would be given a "limitation on the cost they could impose on firms in a given year." Publication of the results would have the additional benefit of educating the public about the actual cost of regulation.

Third, import restrictions should be relaxed. Assuming that the goal of trade restraint is temporarily to cushion the effect of imports on domestic workers and not to protect inefficient U.S. industry indefinitely, Crandall suggests subsidizing displaced workers rather than increasing import prices (quotas, tariffs, and the like). He estimates that consumer prices would be reduced between 0.1 and 0.2 percentage points by removing restrictions on imported steel, sugar, and meat.

Finally, Crandall views the minimum wage as an expensive (and indirect) way of providing aid to low-income workers—and, indeed, as one whose main beneficiaries are often "groups who compete in the labor market with these

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less fortunate workers." Income would be more efficiently redistributed and prices would be reduced (by about 0.2 percentage points of the 1978 increase in the minimum wage) if a wage subsidy were paid to firms that employed workers from certified low-income families.

Crandall demonstrates that the rate of increase in prices could be significantly reduced if the government made these kinds of changes in the means of achieving stated social objectives. And he argues that even if the effect on inflation is short-lived, there will be real gains in economic efficiency.

The Courts and the Spending Power

"The Judicial Power of the Purse" by Gerald E. Frug in *University of Pennsylvania Law Review*, vol. 126 (April 1978), pp. 715-794.

Whatever controversy may continue to surround the activities of the federal courts in other areas, recent decisions ordering dramatic changes in the operation of state prisons and mental hospitals are really a class apart. The author argues that these "institution" cases ought to be of special concern because they "require action by the legislature to raise or reallocate funds and, once that is accomplished, detailed judicial supervision of the executive's efforts to implement the changes mandated by court decree." In short, says Gerald Frug, formerly health services administrator for the City of New York and now a professor at the University of Pennsylvania Law School, such cases directly preempt the necessary political balancing by legislatures and the technical judgments of state officials—often in spectacular fashion.

In one Louisiana case, for example, a federal court order forced the state to appropriate $106 million for capital improvements on a single prison—though the total annual capital outlay *for all prisons in the state* had not previously exceeded $1 million. In one of the most dramatic cases dealing with the rights of patients at a mental hospital, the court ordered that no more than six persons be confined to one room, that each patient be provided specified clothing and furnishings, that toilets and showers of sufficient number and meeting detailed specifications be installed, that day room and dining facilities meet specific size and furniture requirements—and then made equally elaborate and detailed requirements for the provision of professional services.

Frug points out that the Supreme Court has not yet overturned, nor explicitly confirmed, such ambitious and detailed findings by the lower courts (ordered so far in some fifteen states). However, he reviews a range of decisions by the Supreme Court in recent years to suggest that the Court may have reservations about the pattern of these cases. For example, the trend of recent restrictive decisions on standing, in Frug's view, suggests the present Court's reluctance to see judicial decision-making substituted for political or democratic resolutions, while certain recent decisions also indicate increased concern for protecting the operating autonomy of the states. Even the desegregation opinions of the Supreme Court—widely regarded as sanctioning wide-scale judicial intrusion on the operating arrangements of local institutions—"demonstrate an extraordinarily patient recognition of the need for local responsibility and of the practical restraints the localities face in achieving compliance with the constitutional mandate."

The broad language of the Supreme Court's desegregation opinions suggests to Frug a more appropriate approach in cases dealing with the rights of prisoners or mental patients. He does not urge the Supreme Court to deny that those who are involuntarily confined retain a constitutional right to decent treatment. Nor does he maintain that the Supreme Court will do so. But he does suggest that the Supreme Court can improve the direction of the law in this area by limiting the role of the courts to declaring the rights involved in general terms—leaving it to the states to devise suitable remedies at their own pace so long as they are acting "in good faith":

> The power to declare conditions unconstitutional is a potent weapon. . . . But if the power of the courts rests principally on their declaration that current conditions are illegitimate, they must take care not to issue orders that make noncompliance excusable and thus legitimate. The likelihood of compliance is undermined, not enhanced, by detailed orders that fail to recognize the constraints on the political process.

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Broadcast Nonregulation

Reluctant Regulators by Barry Cole and Mal Oettinger (Reading, Mass.: Addison-Wesley Publishing Company, January 1978), 288 pp.

The Communications Act of 1934 authorizes the Federal Communications Commission to regulate wire and wireless communications (interstate and foreign) in "the public interest, convenience, and necessity." Far from clarifying the meaning of this vague charge over the years, the FCC's hesitant approach to regulation in the broadcasting field has, according to Cole and Oettinger, simply increased the murkiness surrounding the public obligations of broadcasters. Barry Cole, professor of communications at the University of Pennsylvania, served the FCC as special consultant on license renewal from 1970 to 1975, and Mal Oettinger is former Washington editor of *Television/Radio Age*.

According to the authors, the commission has not enforced its policies rigorously or consistently, nor has it announced clear programming requirements for radio and television stations. Thus while often urging upon stations the importance of broadcasting "public service announcements," it has never specified a minimum obligation for license renewals (even though stations vary enormously in how often and when they carry these announcements). Similarly, while consistently stressing the importance of local programming, the commissioners did not announce until 1976 that they would personally review all license-renewal applications of those commercial television stations proposing to devote less than 5 percent of their broadcast scheduling to locally produced programs. Then, in the two years after adopting this requirement, the FCC did not review a single license on these grounds, because the requirement was so undemanding (referring, for example, only to *proposed* scheduling rather than actual on-the-air performance).

Cole and Oettinger report that the FCC has almost never penalized broadcasters for failing to live up to the scheduling plans outlined in their license-renewal applications. And failure to meet programming commitments is only one example of unpenalized failure. The FCC has not penalized too many commercials or too little nonentertainment matter.

Indeed, in a wide range of regulatory matters, official FCC policy affords little guide to FCC practice in fact, fundamentally because that body is so reluctant to deny licenses to operating broadcasters. Between 1934 and mid-1977 the FCC revoked or denied renewal of less than 150 licenses, many of them for small radio stations with extreme engineering problems. A formal hearing to consider denying a license is regarded as almost as bad as an actual denial and is almost as rare: out of nearly 3,000 broadcast license-renewal applications processed by the FCC in fiscal 1976, only 23 were set aside for formal commission hearings. No renewal has ever been denied solely because of "failure to meet community needs and problems," too many commercials, too few public service announcements, or insufficient nonentertainment matter—or a combination of these programming misdeeds.

Moreover, although the FCC may impose fines for lesser infractions, it is erratic in assessing them. Cole and Oettinger observe that "when dealing with renewals the FCC practices regulation by a nod and a wink. The unlucky broadcaster who runs afoul of the FCC's elastic standards may justifiably feel singled out. Members of the public are uncertain just what they have a right to expect from the licensee charged with serving their interests."

In the authors' opinion, several factors account for this situation. FCC commissioners (and young staff lawyers), well aware that a majority of their predecessors have gone on to find their livelihood within the broadcast industry (or "communications bar"), may be reluctant to antagonize prospective colleagues. Even the most conscientious commissioners must be concerned about delicate First Amendment issues, about courts' overturning their decisions on procedural grounds and, perhaps most of all, about Congress's limiting the FCC's authority in response to some particularly controversial ruling. Broadcasters, for obvious reasons, are acutely important constituents for congressmen, and the industry as a whole is well-organized and well-positioned for lobbying purposes. Cole and Oettinger conclude that sudden and dramatic change is unlikely but warn that the future of public regulation in this volatile area is impossible for anyone to predict with assurance.

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Politics and the FCC

The Politics of Broadcast Regulation by Erwin G. Krasnow and Lawrence D. Longley (New York: St. Martin's Press, 1978), 213 pp.

This book was written by Erwin Krasnow, general counsel of the National Association of Broadcasters, and political scientist Lawrence Longley of Lawrence University because, in their view, the "political aspects of regulation" have been neglected. The book analyzes the FCC regulatory process to see "who gets what, when, and how."

The first of the book's two parts begins by explaining the historical development and basic characteristics of broadcast regulation (chapter 1). Ever increasing radio communication in the early 1920s resulted in what the authors term an unprecedented phenomenon — the "broadcasting industry itself requested governmental controls to eliminate the audio chaos caused by unregulated radio operations."

Since then Congress has maintained a strong influence over FCC policy, although rarely mandating specific FCC action through legislation. According to Krasnow and Longley, the absence of substantive guidelines—the Communications Act of 1934 is notoriously vague—makes the commission "all the more vulnerable" to other forms of congressional influence, like investigation and the withholding of appropriations. The FCC faces the problem of making policy decisions "when the *wishes* of Congress are quite unclear, but its *presence* very real."

For example, the FCC's primary form of control over broadcasters is its licensing authority and thus stations' license-renewal proceedings. (Other regulatory agencies are primarily charged with regulating profits and prices, but Congress specifically denied the FCC this authority.) However, the broad statutory language requiring the agency to find "public interest, convenience, and necessity" before granting a station's license leaves the FCC vulnerable to a congressional majority that might decide, later, that the FCC's interpretation "is not what *we* mean by the public interest."

Chapters 2 and 3 describe the six participants in the politics of broadcast regulation: the Congress, the FCC, the industry, citizens' groups, the courts, and the executive branch—with the first three traditionally paramount in policy formulation. In the authors' opinion, this exclusive club of three was considerably expanded in 1966 when the U.S. Court of Appeals for the District of Columbia unanimously ruled that the Office of Communication of the United Church of Christ had the right to participate in the license-renewal proceedings of Station WLBT-TV. Until that time, only those with a "demonstrable economic stake" (narrowly defined) had been allowed to participate directly in the formulation of regulatory policy. Seizing on this new opportunity, other citizens' groups have focused their efforts on representing the public before the FCC, the Congress, and the courts. The authors note that the courts are particularly sensitive to citizen participation because, "whereas the FCC and the Congress are most often influenced by politically powerful and wealthy groups, the courts may be influenced almost as easily by a single individual or very small groups as by a large and powerful interest." Thus, the role of courts and of citizens' groups in FCC regulatory matters has grown concomitantly.

The second part of the book consists of five case studies that attempt to flesh out a model of the politics of regulation developed in part one. The case studies—which include discussions of the way policy was arrived at and which participants played important roles —are (1) the 1945 FCC decision to move the FM radio frequency allocation from the 44-megacycle range to the 88-to-108 megacycle band, (2) the 1962 All-Channel Receiver Bill, an attempt by Congress to spur the development of Ultra High Frequency (UHF) television, (3) the FCC's 1963 proposal (subsequently dropped) to restrict the number of commercials a station could broadcast, (4) the FCC's efforts in the 1970s to establish a comprehensive procedure for handling license-renewal challenges, and (5) the FCC's responses to the dramatic increase in citizens' band radios in the mid-1970s.

The authors conclude from the case studies that the commission "seeks modest goals, is flexible in its policy choices and sensitive to feedback, directs its attention to immediate problems in a series of . . . sequential steps, focuses on bottlenecks, and limits its consideration to proposals which are, in its view, only incrementally different from existing policies."

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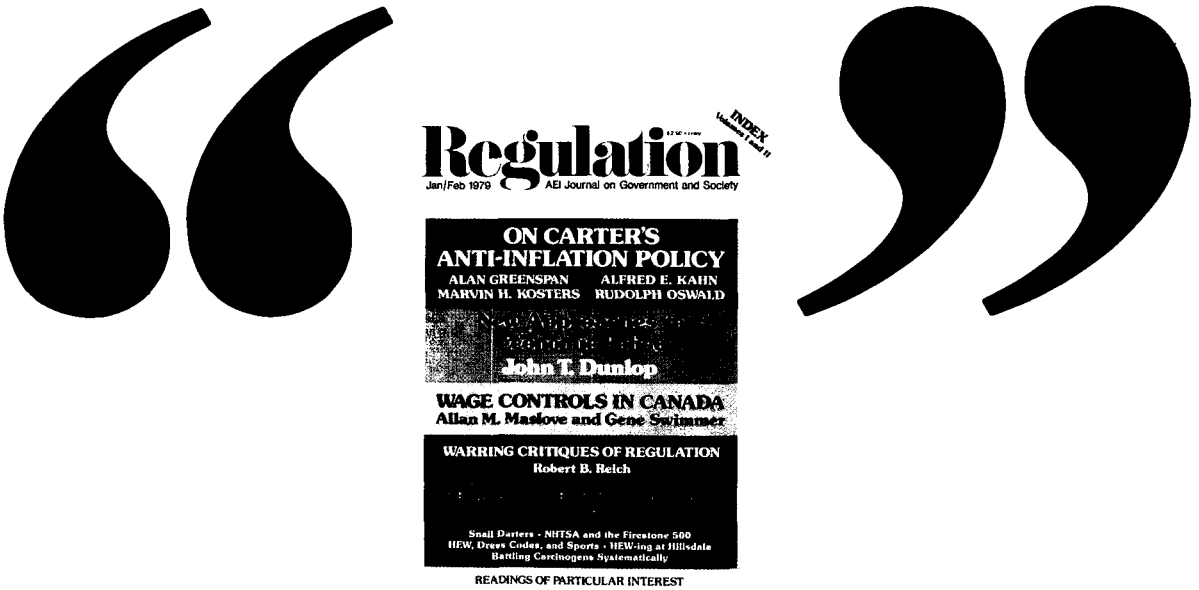

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